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STUDY OF FEDERAL EMPLOYEE LOCALITY PAY

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STUDY OF

FEDERAL EMPLOYEE

LOCALITY PAY

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STUDY OF FEDERAL EMPLOYEE LOCALITY PAY

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STUDY OF FEDERAL EMPLOYEE LOCALITY PAY

TASK 1: *Assessing and Analyzing Critical Federal Pay Determinants*

TASK 1 - ASSESSING AND ANALYZING CRITICAL FEDERAL PAY DETERMINANTS

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APPROACH TO THIS TASK

The federal pay program has a long history that can be traced back to the earliest days of the republic. The program has been subjected to periodic review and occasional revision, and each time the documentation has been extensive. It is essential to understand the recurring themes and the situational factors that interacted to influence decisions that have affected the program. Thus, the history clearly influences decision-making and limits the range of alternatives currently.

At the same time, it is fundamentally important to appreciate the dynamics and immediacy of the current situation. All salary programs are designed to achieve a basic purpose: to attract and retain an appropriately qualified work force. In the case of the government, this involves 1.4 million employees who must decide if the government represents the best employment opportunity, given their individual skills, experience and career interests. Workers always have other employment alternatives where the compensation program can be readily modified to respond to changing labor-market circumstances. Despite the well-documented history, the government has an ongoing, need to maintain an adequate work force, and that makes it imperative to maintain a "competitive" pay program.

In response to the mandate for this Task, we have worked to understand both the historical and the current factors affecting the government's ability to develop, implement and maintain an effective compensation program. This involved a review of numerous published reports and books. Fortunately, several recent reports written as background for the Volcker Commission were made available. In addition, we met with individuals, both in and outside of government, who could help us understand the current situation. The history of the past ten years has a direct bearing on today's problems, and a number of the individuals, with whom we met, were either observers of or involved in the decision-making processes that shaped this period. Other individuals are in positions where they can influence or control the future direction of the program.

More than 200 individuals have now been involved in meetings to discuss the current situation. Most live and work in Washington, but we also met with Federal Executive Board groups in New York, Philadelphia, Atlanta, and Kansas City. The organizations with which these individuals are associated are listed in Exhibit I. Virtually every federal department and agency has been represented in at least one of these meetings. In addition, we have informally discussed specific issues and have been able to refine ideas with many individuals across government.

In each meeting we have explained the scope and objectives of the project. Significantly, everyone agrees that the white-collar salary program is in need of substantial revision. Moreover, no one has argued against the "locality pay" concept. To be sure, the participants in these discussions were reacting to a concept that was, at the time, not defined in specific, operational terms, but the concept of locality pay was widely supported.

While the RFP and contract have used the locality pay phrase, the objective as set forth in meetings at the Office of Personnel Management (OPM) was to explore the feasibility of a "market sensitive" pay program. Through our discussions, we understand that the meaning of "market sensitive" pay goes beyond locality pay, and is someplace between a "market-based" program and the current program. With a market-based program, jobs are assigned to salary ranges that ensure they are paid competitively, without regard to internal equity. However, it is apparent that internal equity is an essential concept in any consideration of the government's program.

HISTORICAL THEMES

Our review of the history of prior efforts to change the white-collar salary program indicates that there are recurring themes involved in the decision process. Although the methods used to administer salary programs have changed over time, the problems have remained essentially the same.

Exhibit II lists the primary studies and reports on the federal pay program along with the legislation enacted since 1919. This historical record documents the steps leading to today's problems.

To place this record into perspective, the first important legislation, the Classification Act of 1923, covered the pay for only 50,000 civilian employees. Before this Act was passed, there was no systematic basis for setting salaries, which resulted in ". . . glaring inequalities and incongruities in salary schedules, pay-roll titles and departmental organization . . . ." The classification system that was introduced at that time established a philosophy and framework for administering salaries that continues today to dominate the white-collar salary program.

- Uniform and consistent administration is a basic objective.

For sixty-six years, a continuing theme has been the need for uniformity and consistency across departments and agencies. Beginning with the 1923 Act, federal pay was increasingly consolidated until the Classification Act of 1949 established a single salary schedule for all white-collar employees.

While early efforts focused on the need for consistent pay administration within a class, this evolved to require consistent treatment of positions across classes based on a comparison of job content.

The concept of a job standard, as it is used in classification, is designed to ensure consistent application of the job evaluation process. As new jobs are created or existing ones revised, they are compared to the relevant standard and classified accordingly. If all departments used these standards properly, the classification process would be applied consistently throughout government. In actual practice, this administrative approach has come under increasing criticism because it has proven to be too expensive to keep the standards updated as occupations have changed.

It is important to note that many occupational interest groups have tried to have their pay administered independent of the General Schedule (GS). Within the GS program there is also the special rate mechanism. Both practices are evidence that the rigid uniformity of the program is not always effective.

- Pay inequities relative to prevailing market rates are secondary to internal comparisons.

The emphasis on uniformity and consistency is closely related to what is generally referred to as internal equity. While government studies have often given recognition to the need to maintain competitive salary levels in situations where turnover is considered to be excessive, the conceptual foundation of the white-collar salary program minimizes the importance of occupation-by-occupation pay comparisons. This is reflected in the use of the survey data reported in the Professional, Administrative, Technical and Clerical (PATC) Survey.

Equity, of course, is an abstract concept or construct that depends on an individual's perspective. In the context of salary administration, the concept refers to a widely-shared belief that an employee's salary should reflect the relative value of his or her job as viewed by the employer. Although salaries are expressed in dollars, it is the relative value (i.e., one employee's salary compared with others) rather than the absolute value that is meaningful. Within an organization, relative

salary levels are best viewed as a hierarchy. From this perspective a job evaluation system, such as the Factor Evaluation System (FES) with its point totals, is designed to determine each job's rank in the hierarchy. Internal equity then implies that jobs, based on their comparative value or importance to the organization, are appropriately ranked in the hierarchy.

The labor market, of course, also establishes a hierarchy of jobs. This hierarchy is driven by the relative supply and demand for different occupations. Over time, the hierarchy shifts as occupations move up or down in terms of relative salary levels. Some corporations rely completely on the market and establish their salary program to pay each job consistent with its market rate. This is normally referred to as a "market-based" salary program.

In most organizations, however, the "equitable" internal hierarchy and market-based hierarchy are not completely consistent, which means the organization would pay selected jobs more or less than the rate dictated by the market. When this happens, the conflict can trigger a variety of personnel problems.

The federal job hierarchy is set forth in Title 5 of the 1949 Act, which describes the characteristics of positions to be assigned to each of the 18 salary grades. This hierarchy was mandated to be consistent with the classification system adopted under the 1923 legislation. Thus, the government has operated with an essentially static job hierarchy for more than six decades.

During this period, wholly new professional fields and new occupations have emerged while others have virtually disappeared. The general level of education and training has significantly increased, and dramatically more sophisticated equipment has come into use. Organization structures and management practices have likewise gone through a transformation.

In light of these changes, it is reasonable to expect relative market rates to shift over time. Salaries for registered nurses, for example, have been rising for several years relative to pay levels for other occupations. Labor markets are dynamic, and most employers manage their salary programs so that they can respond quickly when recruiting or retention problems become evident.

The government's static hierarchy exists in sharp contrast to this normal practice. While the PATC survey data is used as the basis for adjusting the General Schedule so that it mirrors the national labor market movement, salary grades and ranges are independent of the prevailing market rates for specific occupations. Changing this practice, of course, will require legislation to modify Title 5.

- There is recognition that the government is competing directly with the private sector for selected occupations, although the pay program is not designed to accommodate this.

The 1919 study that preceded the 1923 Act noted the government was experiencing high turnover among scientific and technical occupations. The problem has never been solved. While it is impossible to know how more competitive salaries would have affected recruitment and retention for these positions, it is reasonable to assume that the quality of the work force would have been enhanced.

The problem is not limited to top scientific or engineering occupations. The government is competing with the private sector for a diverse group of occupations, from nurses to real estate specialists.

In a competitive market, it is common for corporations to establish above average pay levels to attract higher calibre employees. Although salary is only one of the considerations in taking or leaving a job, there is a belief that relative salary levels are an important issue in salary planning. If higher salaries facilitate the recruitment and retention of better qualified employees, the converse is also true.

Although this has been recognized for at least 70 years, the government has never been willing to deviate from the prescribed internal hierarchy to address the problem.

- Jobs with similar duties and responsibilities are to be treated on the same basis throughout the government (at least for employees covered under the General Schedule).

A key issue in salary planning is the linkage between labor markets and prevailing rates and the organization's salary structure. The most common strategy is to establish salary ranges that provide for average salaries relative to average market pay rates, and this is generally comparable to the government's use of the PATC survey data. By relying on this strategy, an employer is at least implicitly assuming that it will be possible for it to attract average employees.

This is undoubtedly a simplistic view of the factors that affect recruitment and retention, especially for the federal government in light of its image as an employer. However, many corporations rely on a "You get what you pay for" compensation philosophy, and set their salary structures at above-average pay levels. On this basis, salary ranges set at the 90th percentile for an occupation would be intended, over time, to attract the best workers in the labor market. This is a staffing strategy consideration. Generally, compensation opportunities in the more successful corporations are more attractive (i.e., pay is higher) although some portion may depend on incentive payments. Relatively few corporations plan their compensation programs based on below- average salaries.

Historically, the government's compensation policy has been based on national average pay levels. This is consistent with its approach to classification. Both ignore the relevance of individual qualifications. With the exception of the advanced in-grade hiring authority for GS-11 and above, there is no formal basis for recognizing that high calibre individuals can command premium salaries within the current pay

program. The government has essentially adopted an inflexible pay strategy that may be contrary to an agency's staffing strategy.

- Federal pay levels should be comparable with prevailing levels in the private sector.

Although it was not until 1962 that this principle was formally adopted as government policy, it has been an ongoing theme since the end of the depression. Earlier the discussion focused on the "living wage" concept, but of course during the 1930's, with its high levels of unemployment, paying employees enough to maintain an adequate standard of living was a progressive pay policy.

Despite the legislative intent, the actual adjustment each year in the General Schedule has been inadequate to maintain comparability. The PATC survey conducted each year by the Bureau of Labor Statistics shows that the overall white-collar salary program has fallen at least 20 percent behind prevailing private sector pay rates. It is all too obvious that the mechanism created to enable the government to maintain comparability is not working. This has created serious problems of recruitment and retention across the country, especially in certain major metropolitan areas.

There are two issues not addressed in the 1962 Act which have become recurring themes. The first of these is the locality pay question. This is actually a historical theme that has been often recognized in federal pay studies. The second is the definition of the labor market to be used in designing the survey methodology. The argument has been made that the federal government is competing within a broader market than the private sector and that the government's salary surveys should include other types of employers. Private sector organizations do not look to a national market for either clerical or technical positions. These occupations are typically viewed as "local market" positions.

One of the more important labor market trends over the past two decades has been the growth in employment of state and local government entities. The contention is that these organizations should be included in surveys to determine prevailing rates. In addition, of course, there are many other types of employers who compete with the federal government in the labor market, including colleges and universities, professional service firms, health care institutions, and not-for-profit associations. Despite extensive debate, there is no consensus on the definition of the appropriate markets, although there seems to be general agreement that the surveys should cover more than just the private sector.

Another issue is the list of so-called "benchmark" jobs. OPM and BLS have relied on a limited list of generic jobs which are found in many organizations. Noteworthy by their absence are specialized positions with narrowly-defined knowledge or skill requirements (e.g., lawyers who specialize in securities law). The more generalized the data, the less valid it is for a specific position.

The annual adjustment mechanism for the General Schedule now focuses narrowly on the increase in the government's policy line. How the pay for specific benchmark jobs compares with prevailing market rates is not an issue, although the differences are taken into account in deriving the overall policy line adjustment. This approach reflects the primary emphasis on the government's internal job hierarchy.

- A national salary schedule results in overpaying employees in some locations and underpaying them in others.

This is not a new issue. Locality pay has been studied and proposed several times but has not been incorporated into the white-collar salary program.

The Federal Wage System has always been based on the locality concept, and it is accepted by both labor and management.

In the private sector, the available survey data for clerical and other non-exempt jobs are universally reported on a local or regional basis. The major surveys do not bother to report results at the national level.

CURRENT ISSUES

The current problems with and concerns about the white-collar salary program have been stated in any number of forums and publications. The overwhelming message from our meetings is that the problems have reached crisis proportions. Although there is relatively little empirical data to document the nature or extent of the problems, no one involved in our meetings disagreed with the critical nature of the situation. While most of the participants in the meetings were hesitant to suggest solutions, but they clearly were aware of the problems.

Significantly, there are decided differences in the perception of the problems from agency to agency, and from location to location. When we met with the group assembled by the Federal Executive Board in Kansas City, the discussion brought out several emerging personnel problems that are presumably related to pay, but it was clear that the situation there was not critical. In contrast, when we met with a similar group in New York, it became all too obvious that the inability to hire adequately qualified workers meant that some federal operations no longer function at planned capacity.

In discussing the problems and possible solutions, we came to understand that the proposed changes were, to some degree, driven by the criticality of the situation. As the problems have become more severe, it has undoubtedly triggered heightened interest in radical departures from the GS program. Many of the proposed changes would result in short-term alleviation of the crisis, but in time could result in new problems. It will be important to assume a longer-term perspective of the government's needs, and avoid overreacting to the immediate situation.

Overall, the primary problem is that government salaries have fallen so far behind the pay levels offered by other employers that it is difficult, if not impossible, to recruit and retain adequately qualified workers in some occupations and in some

locations. This problem exists throughout government at all organizational levels and, presumably, in all departments and agencies.

- The problems will become progressively more severe over the next several years.

The personnel managers report that their agencies are experiencing increasing turnover, which they attribute to the recently adopted Federal Employees Retirement System (FERS). The older Civil Service Retirement System (CSRS) is often viewed as a so-called "golden handcuff" that makes it difficult to justify early termination, but an objective in adopting FERS was to establish a more portable pension. As the number of employees covered under FERS increases, the level of turnover should also increase. This will be true even if salaries are increased to more competitive levels, though employees will, presumably, have less reason to terminate.

When this phenomenon is combined with the work force projections over the next decade, as discussed in the report Civil Service 2000, the staffing shortage could rapidly become a problem of sufficient magnitude to threaten the continuation of vital government operations and services.

- There is a need for the delegation to the agencies of some pay program accountabilities and for increased flexibility in program administration.

Driven largely by their sense of frustration, at least the larger agencies want the delegated authority to develop and administer their own pay programs. They believe that they would be able to operate better with a salary program over which they had greater control.

In part, the interest in developing their own programs is a reaction to the rigidity of the current program. The personnel managers repeatedly make the point

that their agencies have unique needs that are not adequately served by the GS program and its associated administrative regulations.

- The classification process is no longer working and needs to be "repaired."

While the argument is often made that classification and compensation are separate functions, the reality is that they are interrelated and function independently only when both are not affected by problems. In virtually all private sector employers, the two functions are combined and managed as a single program.

As the compensation problems have become more severe, classification decisions have been distorted by the need to maintain competitive salaries. The personnel managers recognize that many positions are overgraded ("grade creep"), but no one fully understands how serious the problem has become. The issues of position management and grade creep are discussed, in greater detail, later in this report.

There are, to be sure, other perceived problems with the classification system. If the salary program is to be revised, it will be important to address some of the concerns with the classification system.

- The regulatory bureaucracy and required paperwork get in the way of day-to-day management actions.

The contrast between the administrative functions required to maintain the government's salary program and that of a typical large corporation is dramatic. While most corporations administer their pay programs with comparable administrative mechanisms (i.e., job evaluation systems, salary increase procedures, etc.), the administrative requirements are not often seen as impediments by both line managers and personnel managers. The administrative function required to maintain an effective pay program necessitates the routine exchange of job and individual

information, and the documentation of personnel actions. OPM should examine regulations to determine whether the reporting requirements currently in place be simplified without the loss of legally-mandated information. Such a review wo be appropriate at the time of a salary program revision.

FEDERAL PAY DETERMINANTS

The determinants of the federal pay program are both numerous and complex. Significantly, they are very different from those that drive the typical corporate program. Despite the commonalities in terms of basic program objectives and design concepts, the only similarity in year-to-year operation is that they both result in paychecks to employees.

For the purpose of this report, we have identified as pay determinants the factors that have contributed to the current problem which are both external and internal to the pay system. If these factors did not exist, the current situation would be significantly different.

While the underlying constant that affects most of the determinants is the political process, there are other dynamics at work in the actual operation of the system which affect how pay is delivered and, which taken together, are significant in their impact. A number of these factors mitigate against the problems created by the pay gap but are so operational in nature as to be generally overlooked.

In the past year, the media attention to the plan to increase congressional, judicial and federal executive salaries illustrated how easily a nonpolitical decision process can be overwhelmed by political considerations. It is not always manifested as a partisan issue but the recognition that key decision-makers tend to reflect partisan positions influences lower-level planning. Moreover, the need at some point to reach agreement at the highest levels of government makes it difficult, and often impossible, to agree on program changes.

- Lack of Agreement on Compensation Philosophy and Program Objectives

The foundation of an effective pay program is the organization's compensation philosophy or strategy, and the compensation program's objectives.

For a corporation, the business strategy dictates a staffing strategy and this, in turn, dictates a compensation strategy--"To recruit and retain these employees, these are the pay levels we need to maintain." This makes it possible to develop specific program objectives. The pay program can then be evaluated based on the objectives.

The compensation strategy is normally discussed and refined by the organization's senior executives and often by the board of directors. The same decision makers are responsible for the organization's business strategy, and for directing the organization toward the achievement of its operating objectives. Over time, the compensation program's objectives need to be reviewed periodically and adjusted to ensure that they are consistent with and support the business strategy.

This planning process is dependent on management's agreement on and commitment to the business objectives. Organizational priorities are dictated by the business objectives. While short-term operating problems may force the organization to reduce planned compensation opportunities, this action is taken with full knowledge that it could, if extended, make it difficult to recruit and retain adequately qualified employees. This approach to planning makes it possible to reach agreement on the need for program changes, and for evaluating alternative program modifications.

Despite the Comparability Acts of 1962 and 1970 and the Civil Service Reform Act of 1978, there is an apparent lack of agreement on the government's compensation philosophy. For the past decade, the program has obviously been a low priority, with little concern for the personnel ramifications. Government would benefit from a renewed commitment to its compensation program.

-Inadequate Program Understanding

Despite the fishbowl quality of program administration, it lacks credibility and is poorly understood. The problem is that it is difficult to define or even to isolate all of the contributing factors. One of the factors certainly is the mechanism used to determine the annual adjustment to the pay program with its narrow focus on the pay gap. Another factor is the influence of the media on everyone's understanding of the pay-related problems. A third factor is simply that the program's size and complexity makes it difficult to focus on specific pay-related issues. Finally, the government's internal communication of the program components could be substantially simplified and improved.

For almost a decade, federal employees have learned repeatedly that they are paid significantly less than their counterparts in the private sector. In Washington at least, it may be safe to assume that this "truth" is universal, and believed by federal employees who are not even covered under the General Schedule. Regardless of the facts, it has been our experience that most employees are convinced they could make significantly more in the private sector.

Our impression is that employees are not even aware of the positive aspects of the program. Everyone focuses on the annual schedule adjustment and forgets the step increase that many also receive. The combination of the two is fully competitive with the average merit increase budget in the private sector (currently 5 percent). They also ignore the value of promotional increases. The promotional increases in government start at roughly the average for the private sector (10 percent) and rise, for two-grade promotions, to almost double this amount.

It is obvious that entry-level salaries are inadequate for many occupations and in many locations, but our sense is that individual federal salaries increase faster than is typical in the private sector, at least in the early years of an employee's career. If it were possible to compare individual salaries for individuals with

equivalent credentials in federal and private jobs, it may be that federal employees are actually close to competitive levels during the period within three to five years from their date of hire. If the data were available to compare career salary histories, particularly for the professional and administrative "two-grade interval" series, it would significantly enhance the stature of federal careers.

From the policymakers' perspective, they see the same disclosures regarding the pay gap, but they also see data regarding recruitment and retention across the country. They also have access to reports on overgrading and the large proportion of employees in the higher salary grades. It is normally assumed that a significant pay gap should result in increased turnover or trouble recruiting; however, except in specific major metropolitan areas, there is little evidence that the problem is nearly as serious as the purported gap would suggest.

The methodology employed each year to measure the gap has lost credibility because the results are not wholly credible. Although the techniques used to compare Federal and private sector salaries have been checked and re-checked by experts, the results are virtually ignored because they are inconsistent with the perceived reality. This inconsistency arises, at least in part, as a result of measuring a national market for clerical and technical employees--a market that does not exist. In fact, the widest variation from location to location is found in these two groups. Therefore, averaging high and low cost areas produces a result which, most likely, has no relevance to any specific local market.

It will be difficult to change the understanding of the situation. It is clear that, until policy makers are provided with more credible information, it will be difficult to develop broad-based support for meaningful change. Similarly, federal employees need a better understanding of how their pay compares with that of other workers across the country who began their work careers with comparable backgrounds. Government would be well served by a communications strategy that accomplished both objectives.

- The Title 5 Job Hierarchy and the Classification System

In defining the types of jobs to be assigned to each grade, Congress has made it virtually impossible for the government to respond to changing labor market conditions. Since the government's job hierarchy was first established in 1923, changes in knowledge, technology, and the organization of work have transformed all but the simplest white-collar jobs. In fact, even the value of college degrees has shifted significantly from the time the hierarchy was established.

The concept of classification and the supporting administrative mechanisms are intended to assign positions to the hierarchy on a consistent basis over time. When the government's systems were developed, they were somewhat ahead of their time (when compared with industrial practices), but they are now dated.

The relative GS grade differences are arbitrary and inconsistent with prevailing private sector practice. This means that even when some jobs are paid competitively, others will be higher or lower than prevailing market rates. The discrepancies make it difficult to develop a consensus on adjusting the salary program.

- The methodology used to adjust the General Schedule.

While the adjustment methodology starts with salary survey data, at no point, other than the first step, do the reported results draw attention to job-by-job pay comparisons. A complicated methodology is employed to transform the job-by-job salary data collected into a usable format for determining the amount of the General Schedule adjustment.

In addition, since the methodology focuses narrowly on the private sector, it severely limits the number of "benchmark" jobs (i.e., those that are comparable across organizations and used for survey purposes). At the higher grades, the

benchmark jobs are limited to a handful of relatively high paying jobs (5 jobs at GS-14 and 3 at GS-15). As an example, lawyers and systems analysts are benchmarks at both GS-14 and GS-15. Although the necessary data are unavailable, we suspect that the employers surveyed for the higher level benchmark positions are limited to the larger corporations. (Very few small firms employ individuals at these levels.)

If the relevant labor market is redefined to include state and local governments, it should significantly lengthen the list of possible benchmark jobs. While there is no survey data available to determine how this will affect the annual adjustment, it should, at the very least, enhance the credibility of the process.

- Occupational Interest Groups

It is hard to modify a pay program without changing the job hierarchy. Even adding or deleting salary grades (e.g., going from 18 to 12) means that jobs will need to be assigned to new grades. This generates concern that some occupations will make out better than others. (e.g., if the grades of all engineers were increased while others remain unchanged).

In the private sector, changing a pay program has the same potential to affect the job hierarchy, but employees generally are not told what the changes mean to other employees. This secrecy makes it easier to introduce change. Moreover, most private sector employees do not have anyone to whom they can turn to if they want to protest announced changes. In the typical private sector organization, the culture supports the need for change if it is for the "good of the organization," so there is relatively little resistance.

The open communication that prevails in the federal sector, especially on issues affecting the federal pay program, means all employees are aware of changes. They can turn to any of several organizations both inside and outside of government

(e.g., unions, employee associations, and professional associations) if they want to protest or modify proposed changes. Several of these organizations have sufficient influence with Congress to prevent change. Consequently, it is extremely difficult to introduce meaningful program modifications.

- Need for Consensus

The absence of an overall compensation philosophy means that each time program changes are contemplated, there is a need to develop a new consensus to support the proposed changes. This inevitably shifts the emphasis from the development of technically sound program changes to ones that are broadly acceptable. It also makes it difficult to develop support for changing the program until there is a crisis.

- "Fed Bashing" and the Image of Federal Employees

Federal employees have been denigrated by spokesmen from all sides of the political spectrum. Presumably, there are still prospective applicants for federal jobs who are interested in the intrinsic rewards of public service, but federal careers are clearly less attractive today than they were a decade or two ago. Surveys of federal executives show that even they do not want to see their children pursue federal careers.

In light of the "fed bashing," it is not surprising that there is inadequate support for raising federal salaries. As the Volcker Commission recently emphasized, it is important, for reasons that go beyond the pay problem, to improve the image of federal workers. This is not an easily resolved problem.

If the public image of federal workers was more positive, it presumably would increase the pool of job applicants and make it easier to develop public support for salary increases.

- Position Management and "Grade Creep."

There is a widely shared perception that there are too many federal employees in the higher salary grades (roughly GS-11 to GS-15). Not only are the percentages of employees in these grades high, but they are increasing from 35 percent in 1974 to 40 percent in 1988. This does not directly affect the structure of the salary program, but it is an important determinant of the costs associated with proposed schedule adjustments.

Although valid comparative data are not available, our experience in designing corporate salary programs leads us to agree that there are an unusually high percentage of employees in the higher grades. The typical corporate organization has most of its employees in the bottom half of the salary structure. It may be that the difference is attributable to the nature of government operations, but there are at least two other explanations. First, it may simply be that it is a result of the "games" that are often played with a classification or job evaluation system. This is the essence of "grade creep." The second explanation is that in organizing the structures, there has been an unnecessary assignment of work to workers at high salary grades. This comes under the position management umbrella, and is very difficult to control without an in-depth audit of the work performed.

The widely accepted belief is that both problems are attributable to the compensation system, and the pressure to maintain salaries which are closer to market levels. Neither problem, however, would "disappear" if salaries were increased--there will always be pressure to inflate salary grades and pay levels. Supervisors and subordinates alike benefit if grades go up over time, and there is no effective control mechanism in place. At the same time, it will be difficult to gain support for increasing salaries that are already considered to be higher than justified by the level of the work performed.

- Breakdown of Trust Among the Key Decision Makers

Over the past decade, there has been a progressive deterioration in the relationships among the organizations that are needed to influence and control the pay setting process. There is a high -level of distrust and inadequate communications. The "major players" have become frustrated, and evidence little interest in continued participation. The decision process has failed.

It is fundamentally important to revive or preferably re-establish an effective mechanism for addressing the federal pay program. Our meetings have convinced us that the disagreements among the players on what has to be done are minor. There will always be a Kabuki theater quality as the decision makers play their public roles, but we would like to believe that they will be able to work together effectively behind the scenes. There is an absolute consensus that change is necessary.

- Budget Deficit

The impact of pay increases on the budget was a concern even when there was no deficit. The government, as with all organizations, has to decide how to allocate available funds, and it is apparent that federal employees are a relatively low priority.

Holding salaries down has direct cost implications but unfortunately it is hard to measure the increased expenditures triggered by employee frustration (e.g., turnover costs, poor performance, substandard applicants). Moreover, these costs are never aggregated so they are never publicized. It would be useful to identify operating problems which were caused by or happened because of situations being mishandled by inadequately qualified workers. As the private sector is aware, "You get what you pay for."

RESPONSE TO SUPPLEMENTAL OPM QUESTION

- Are changes needed in areas outside the pay setting process itself to improve the system's responsiveness to market conditions?

It would, of course, be highly advantageous to shield the process from political influence. We appreciate that this is virtually impossible, but the program has enough baggage of own. At least two statutorily conceived committees of prominent citizens, the Quadrennial Commission that reviews judicial, congressional, and executive salaries and the Advisory Committee on Federal Pay that reviews the General Schedule program, are intended to accomplish this, but it is all too obvious that the process is not working. This experience does not negate the value of a regular review by a cross-section of prominent individuals who can be expected to devote sufficient time necessary to understanding the program.

Although any form of cash payment is related to the pay setting process, as long as the basic program remains unchanged, it would be advantageous to authorize the payment of recruiting and retention bonuses. Although we feel strongly that bonus payments do not represent a long-term solution, the government needs the flexibility to make supplemental lump-sum payments to help recruit or retain key people. When used to retain individuals in high demand fields, the payments would be similar to the so-called "golden handcuffs" that play an important role in corporate executive compensation programs.

It would also be advantageous for the government to address the communications problem. While OPM should take the lead, each department and agency should assume responsibility for developing an effective internal communications program. Unfortunately, only agencies in the high pay areas--New York, Los Angeles, and Boston--have taken the time to assemble and communicate information that shows how federal pay levels compare with local market levels. In many locations across the country, this would send a positive message to employees

that could serve to improve employee morale and offset the decidedly negative message sent by requests for special rates.

The communication strategy should focus on how federal salary ranges for selected occupations compare with prevailing local levels. The information is readily available in numerous published surveys. The communications strategy should also publicize the rate of individual promotions and incentive awards granted--the good news. The government still offers satisfying and exciting career opportunities, and we sense that an effective communications strategy at the agency level could diminish the importance of the pay gap.

EXHIBITS

Exhibit I

DEPARTMENT/AGENCY MEETINGS

Group Meetings, Personnel Managers

- Interagency Advisory Group (IAG)
- International Personnel Management Association, Federal Division (IPMA)
- Independent and Regulatory Agency
  Personnel Directors Group

Private Meetings, Personnel Managers

- Department of Air Force
- Department of Navy
- Department of Labor
- Department of Transportation
- Department of Treasury
- Defense Contract Audit Agency
- General Services Administration
- Internal Revenue Service
- National Aeronautics and Space Administration
- National Institute of Health
- National Science Foundation
- Smithsonian Institution
- Veterans Administration

Federal Executive Board, Group Meetings

- New York
- Philadelphia
- Atlanta
- Kansas City

Technical Resources

- Bureau of Labor Statistics
- Prevailing Rate Advisory Committee
- OPM, Office of Classification
- Alan K. Campbell, former Director, OPM

Union Organizations

- American Federation of Government Employees
- National Treasury Employees Union
- National Federation of Federal Employees
- National Association of Government Employees
- Public Employee Department, AFL-CIO

Other Employee Organizations

- Senior Executives Association
- Federal Bar Association
- Federal Managers Association
- Professional Managers Association

Non-Government Organizations

- National (Volcker) Commission on the Public Service
- National Academy of Public Administration
- Carnegie Commission on Science, Technology and Government

Exhibit II

MAJOR STUDIES/LEGISLATION DEALING WITH FEDERAL WHITE-COLLAR PAY PROBLEMS/REFORMS

Year	Official Title	Common Title
1919	Act establishing the Joint Congressional Commission on Reclassification of Salaries	
1921	Executive Order directing the Bureau of Efficiency to develop a uniform system of position classification and efficiency ratings to be implemented by all departments. Eighteen salary grades, with most having seven steps, were prescribed.	
1923	Classification Act of 1923	
1937	President's Committee on Administrative Management Report--To the President: Administrative Management in the Government of the United States Ramspeck Act of 1940.	Brownlow Committee
1949	Commission on Organization of the Executive Branch (1947-1949) Report--To the Congress: Personnel Management Class Act of 1949.	Hoover Commission I
1953	Senate Committee Study Report: Administration of the Classification Act of 1949 and the Compensation Process Established by the Act (Senate Doc. 34, 83rd Congress, 3-18-53)	

1955	Commission on Organization of the Executive Branch (1953-1955) Report--To the Congress: Personnel and the Civil Service Major Recommendations: Improve efficiency of Government; Distinguish between top career and policy positions; Improve employee development; and Improve performance evaluation.	Hoover Commission II
1957	Committee on Scientists and Engineers for Federal Government Programs Report: To the President	
1957	Defense Advisory Committee on Professional and Technical Compensation Report: Plan of Action to Attract, Retain Professional, Technical, and Managerial Employees for Defense, Vol. I--Civilian Personnel	Cordiner Committee
1957	Interdepartmental Committee on Civilian Compensation Report: On Civilian Compensation in Executive Branch of the Federal Government	O'Connell Committee (J.T. O'Connell, U.S. Dept. of Labor, Chair)
1961	Joint Studies (BOB, CSC, Office of Special Assistant to the President for Personnel Management) of Classification Act Pay Reform (1958, 1959, 1960) Report: Classification Act Pay Reform: Report on Joint Studies	Lehman-Mc Afee Milkey Committee
1962	Federal Salary Reform Act of 1962 Message: From the President (Budget Message, January, 1962)	
1963	Advisory Panel on Federal Salary Systems Report: House Committee Print, (8-16-63)	

1965	President's Special Panel on Federal Salaries Report: (Summarized in) Pay Increases for Certain Civilian Employees and Members of the Uniformed Services (House Doc. No. 170, 89th Congress, 5-12-65)	Folsum Panel
1967	Federal Salary Reform Act of 1967	
1969	Subcommittee on Position Classification, House Committee on Post Office and Civil Service Report: Job Evaluation and Ranking in the Federal Government (House Report 91-28, 2-27-69) Major Recommendations: Improve position classification in Federal Government; Educate personnelists and managers; Simplify system: "one service-wide ranking system;" Increase funds for salaries; and improve job evaluation system.	Hanley Subcommittee
1970	Pay Comparability act of 1970	
1972	Job Evaluation and Pay Review Task Force Report--To the CSC: Final Review of the Task Force. Major Recommendations: Improve position classification and pay systems of Government; Optimize external alignment locality rates; Restructure General Schedule to meet pay policy needs; Replace GS with 6 systems; and maintain internal alignment over broad bands.	Oliver Task Force

1973	Test and Implementation Group Report: Of Project to Develop, Test, and Evaluate an Improved Approach to the Evaluation of Non-Supervisory Positions at GS-1 thru GS-15. Major Recommendations: Develop, test, validate a factor evaluation system for classifying General Schedule jobs; CSC should adopt a factor evaluation system within framework of existing General Schedule statue; and CSC should implement FES gradually as it completes occupational studies and issues new standards.	TIG
1975	CSC Studies of Federal White Collar Compensation Reports: Redesigning the General Schedule (CPG 76-2); Total Compensation Comparability (CPG 76-5); 3 other volumes Major Recommendations: General Schedule split into 4 separate services, each with its own pay system and job evaluation plan; and salaries for clerical and technician services based on local pay surveys (others nationwide).	"Ash Letters" Projects/CSC Studies
1976	President's Panel on Federal Compensation Report--To the President. Not officially published. Major Recommendations: Split GS into 2 services (Clerical/Technical and Professional, Administrative, Managerial, Executive); Total Compensation Comparability (TCC); and clerical locality pay.	Rockefeller Panel

1977	Federal Personnel Management Project Report: Final Staff Report (12-77) Major Recommendations; Structural reforms in personnel management; Establish SES; Split General Schedule; Locality pay: clerical and technical; and include state/local data in comparability studies. Portions of this appeared in the Civil Service Reform Act of 1978.	Ink Task Force
1978	Civil Service Reform Act of 1978	
1979	Federal Employees Compensation Reform Message--From the President	CSRA II (Not enacted)
1980	American Society for Public Administration Report: Federal Compensation Reform, An Examination of Issues Major Recommendations: Total compensation comparability should be central principle to determine Federal compensation; State/local government data should be included in comparability measurements; Most of Federal white collar work-force should be on locality pay; and Blue collar pay: technical adjustments and abolition of Monroney Amendments.	ASPA Study
1981	Classification Task Force Report: A Federal Position Classification System for the 1980's Major Recommendations: Continue the General Schedule; Establish locality pay schedules for some groups; Strengthen supervisory relationships and pay; and improve content of classification qualification standards.	Forrer Task Force

1981	Federal Pay Comparability Reform Letter--To the Speaker of the House, Transmitting Legislative Proposal	Reagan/Devine Bill (Not enacted)
1981	President's Advisory Committee on Federal Pay Report: A Decade of Federal White Collar Pay Comparability, 1970-1980	
1982	Consortium on Federal Pay Reform Report: A Study on Pay Reform Issues (Public Administration Service, Inc.) Major Recommendations: Change the organizational and procedural aspects for setting/adjusting Federal pay; Support the principle of TCC for Federal pay-setting; Divide General Schedule into 2 more homogeneous occupational groupings, with national concept of "special occupations or groups"; and expand and modify merit pay coverage and provisions.	
1983	National Academy of Public Administration Study Report: Major Recommendations: Update classification standards and focus on journeyman levels; Delegate classification authority to supervisors and managers; and cut red tape.	NAPA Study

1983	President's Private Sector Survey of Cost Control in the Federal Government Report--To the President Major Recommendations: Simplify standards; Update standards on 5 year cycle; Consolidate classification and pay organizations in OPM; Correct overgrading within 3 years; Push position management; Provide agencies with technical advice and evaluation of programs; OPM/OMB protect budget funds of agencies doing good position management. Develop labor market philosophy; and design market based pay system.	Grace Commission
1984	Cabinet Council on Management and Administration; U.S. OPM; President's Pay Agent Report: Reforming Federal Pay: An Examination of More Realistic Pay Alternatives. Major Recommendations: Modify annual comparability survey to include: -establishments with 50 or more employees -the non-profit sector and other presently excluded industries -State and local governments for informational purposes until authorized by law; Improve survey job list and treatment of data; and expand special pay rate authority.	CCMA Working Group
1984	Hay Management Consultants Report: Study of Total Compensation in the Federal, State, and Private Sectors (House Committee Print, 98th Congress)	Hay Study

STUDY OF FEDERAL EMPLOYEE LOCALITY PAY

TASK 2: *Gathering Information On Pay Setting Practices In The Non-Federal Sector*

TASK 2 - GATHERING INFORMATION ON PAY SETTING PRACTICES IN THE NON-FEDERAL SECTOR

CONTENTS

APPROACH TO THIS TASK 1

RESPONSE TO SUPPLEMENTAL OPM QUESTIONS 2

APPENDIX 10

- 1989 Survey of Locality Pay Practices in Large U.S. Corporations

APPROACH TO THIS TASK

Our approach to this task was to conduct a survey of salary management practices in large corporations. The list of companies invited to participate included 248 that a database of corporate information indicated had at least 25,000 employees. All are "national establishments with regional and local sites and a geographically dispersed work force."

A survey questionnaire was developed in conjunction with the OPM staff, and mailed in March. Enclosed with the questionnaire was a letter from the current chairman of the American Compensation Association, the primary professional organization in the compensation field, asking recipients to participate.

RESPONSES TO SUPPLEMENTAL OPM QUESTIONS

Our responses to these questions are based on the current large corporation survey, a similar 1987 survey conducted for the U.S. Advisory Committee on Federal Pay (which had 1,415 participants), and our experience as consultants.

- How do non-federal establishments decide what their pay system structure should be and how different pay schedules are related?

The pay system structures in most large corporations have evolved over time, and generally conform with a framework and approach to salary management that is virtually universal. That framework provides for a salary "structure" that is a series of interrelated and overlapping salary ranges.

This concept has been widely used for several decades, and there has been little meaningful experimentation or testing of alternative concepts.

Virtually all large corporations have separate salary structures for their "exempt" and "nonexempt" staffs. These terms have been used since the enactment of the Fair Labor Standards Act (FLSA) which requires premium pay for non-exempt employees for hours worked beyond 40 in a work week. As a result of the legal distinction and concomitant compliance requirements, corporations established and have continued separate salary programs for several decades. In general the nonexempt distinction applies to the occupations included in the federal Clerical, Technician and Other series.

Many large corporations also maintain separate exempt salary structures for separate industry or business operations. The logic generally is that the compensation program, including cash incentives, has to be designed to be competitive within the industry. The day-to-day control of the program is in some case delegated to the human resource staff in the business unit (e.g., group division

or subsidiary), and then is likely to be independent of other compensation programs maintained by the parent corporation.

The common thread that runs through virtually all corporate compensation programs is the basic view that salaries need to be set and administered in relation to prevailing or "competitive" pay rates. Corporations typically have an explicit or implicit compensation strategy that, at a minimum, sets forth where (i.e., how high) the corporation wants its pay levels to be relative to prevailing rates. In keeping with the "You get what you pay for" logic, corporate decision makers frequently establish a specific market level as a goal or objective for the salary program. Statements such as the following are common in corporate compensation strategies.

"It is our policy to . . .

- be competitive (average) within the communities where we operate."
- pay equal to the leading corporations in our industry."
- provide above average compensation opportunities (e.g., 75th percentile) relative to our product market competitors."

However the policy is stated, it provides a basis for defining and studying relevant labor markets. Once there is agreement on the relevant markets, it is the responsibility of the compensation analysts to identify sources of survey data and to determine for benchmark jobs the compensation level that is consistent with the organization's strategy. These pay levels are in turn used to establish the salary structure.

The corporation's compensation strategy establishes the relationship between pay schedules. In a highly diversified and decentralized firm, autonomous business units could conceivably establish independent structures. At the other extreme, there are highly centralized corporations that pay all exempt employees within a single salary structure.

There is not necessarily any relationship between the exempt structure(s) and the nonexempt structure(s). They are generally based on different survey sources and reflect somewhat different format principles (e.g., differences between midpoints). From the corporation's perspective, these are independent considerations.

- How are surveys designed regarding scope, area, jobs, etc.?

It is important to note that there are at least four different types of surveys, with the variations related to (1) the sponsor and (2) the targeted participants. The most widely used surveys are designed to be broadly relevant to the full spectrum of employers. The BLS is the most prominent organization conducting surveys of this type, followed by Wyatt's Executive Compensation Service (ECS), and organizations such as the Administrative Management Society (AMS). With these surveys, the survey instrument and data collection process is designed by the sponsor, with little or no input by prospective participants. The second type of survey is sponsored by local personnel associations (e.g., The Washington Personnel Association) and most local employers are invited to participate. Although the survey is typically designed and conducted by a voluntary group of personnel managers, it has to be sufficiently generic to make sense for the full spectrum of local employers. The third type is sponsored by an industry association (e.g., the Chain Restaurant Compensation Association). The benchmark jobs are selected and defined using specific industry terminology, which may make it difficult to compare results with other surveys. Again, there are volunteers who design and otherwise assume responsibility for the survey. Finally, there are private surveys conducted by individual companies and by consulting firms for a specific client, and designed to meet the client's specifications.

Surveys at the executive level are based on common positions (e.g., Chief Financial Officer). The scope of the position is measured by a variety of means, depending on the position. For example, the scope for the CFO might be the firm's

asset size (in banks) or annual sales (in most other for-profit organizations) while the scope for the Vice President - Human Resources would usually be number of employees in the organization.

The geographic scope varies widely and ranges from a national market at the executive level, to a regional market at the professional level to a local market at the clerical level.

- Are decisions made centrally or locally?

This depends on the firm's business strategy and generally operating philosophy. In most firms the decisions involved in the program planning process are centralized. These decisions include:

- the compensation strategy;
- the conceptual framework for the salary structure;
- the method used for job evaluation;
- the policies governing salary actions; and
- the annual salary structure adjustment.

If the planning process is decentralized, the corporate headquarters will normally retain the authority to approve operating unit plans.

Once the salary program is planned, it is common to decentralize responsibility for day-to-day administration. This includes the evaluation of new or revised jobs, the approval of starting salaries and individual salary increases. Our survey shows, however, that the personnel function generally has a role in the review process governing these actions. Moreover, it is important to appreciate that the administrative mechanisms and policies are typically developed on a centralized basis.

- What is the role of unions?

Very few corporations have unions involved in the pay setting process for white-collar workers. Our survey confirms this conclusion.

Where unions are involved (e.g., the auto industry), there is a likelihood that workers will be paid under a national structure. Our survey indicates that these corporations believe that salaries dictated by these contracts are above competitive levels.

If there is a collective bargaining process, we presume the union will be involved in all aspects of the pay setting process.

- What is the nature and extent of pay forecasting for budget planning?

Budget planning in most corporations is relatively straightforward and based on the underlying compensation objective--to maintain a competitive program. At its simplest level, the budgeting process focuses on the percentage increase plans of other employers, and assumes that it will be important to develop a budget that is generally consistent, in percentage terms, with these plans. It is for this reason that the American Compensation Association, many personnel associations, and human resource consulting firms conduct salary budget surveys in the summer and fall.

Each salary program is generally budgeted separately, depending on market information relevant to the program. This means that, for example, the exempt and nonexempt program budgets provide for different increases.

Our survey confirms that the comparative salary levels of other employers is the primary criterion for salary program planning. This was followed closely by the firm's financial performance. Significantly, of the five criterion listed, cost-of-living was the least important.

The weakness in this approach is that it ignores the firm's general position relative to prevailing market levels as well as the firm's compensation strategy. If the firm's program is already well below the market or, for that matter, significantly above the market, a merit increase budget that is competitive--equal to the plans of other employers--will maintain the same relative market position at the end of the new fiscal year. To change the firm's relative market position, of course, the budget needs to be more or less than the budgets of other employers in the same labor market.

The government's current budgeting process is in some respects better than the typical corporate approach but it has lost credibility. An important issue is the definition of the relevant labor markets which, of course, is a primary reason for this study. If the salary program is modified to incorporate the locality concept, the budgeting process would be based on local market data. Moreover, it is anticipated that the market definition should be broadened to include state and local governments as well as other not-for-profit employers. It would also be advantageous to update or revise the survey data before using it in the budgeting process.

- Are pay incentives for movement to other cities included in base pay?

Typically, payments associated with relocation are separate payments and continue for a limited period (e.g., two or three years).

Our survey indicates that virtually all relocated employees work in professional or managerial positions, where there is normally a national salary structure. The pay incentives are designed to induce employees to accept relocation and to cover the additional expenses incurred typically in the transition to life in the new location.

Most of the relocations at these levels (85%) involve promotions, so there is an added monetary incentive to accept the promotion.

- If differentials are paid, how are geographic boundaries for any additional pay decided?

Local salary programs typically have imprecisely defined boundaries. Often these boundaries are indirectly defined by the locations of the employers that participate in generally-used surveys.

As our survey shows, there is no dominant prevailing practice.

It is important to emphasize that even the largest corporate employers do not have large numbers of employees in many different locations. There is no compelling reason to establish rigid rules for defining local areas; the rules for defining each location can be uniquely determined for each location.

Our experience suggests that:

- if the primary work location is "downtown," the area is likely to be limited to other similarly located employers;
- if the primary work location is in the suburbs of a major city, the area is likely to be limited to other suburban employers, unless the only available data covers a broader area; and
- if the primary work location is in a rural area, the area will be defined by the availability of survey data.

- How do pay practices vary by local, regional, or national occupational groupings?

The only apparent distinctions are between exempt and nonexempt and, within the exempt group of occupations, between the executive/managerial positions and the non-managerial positions.

The nonexempt occupations are almost always paid under local salary programs. The salary structures used in these programs are similar to those used for exempt occupations, but typically have smaller ranges, 35 to 45 percent from minimum to maximum, than the exempt structures, where the ranges vary from 50 to 60 percent or more.

At the executive/managerial level, the structures provide for somewhat larger ranges--60 to 70 percent. It is also common for these positions to maintain an integrated, cash compensation program, with base salary combined with annual performance-based incentive payments.

In other respects, the practices used in designing and administering salary programs do not vary by occupations.

APPENDIX

1989 SURVEY OF LOCALITY PAY PRACTICES IN LARGE U.S. CORPORATIONS

Summary Report

Sponsored by

U.S. Office of Personnel Management

Conducted by

THE *Wyatt* COMPANY

1700 One Penn Center
Philadelphia, PA 19103

List of Participants

Abbott Laboratories
Aetna Life & Casualty
Allied-Signal Inc.
American Airlines
American Cyanamid
American Express Company
Ameritech
Amoco Corporation
Anheuser Busch
ARA Services, Inc.
AT&T Corporation
Bank of America NT & SA
BellSouth Corp
Beverly Enterprises
BP America
Brunswick Corporation
Burlington Industries
Campbell Soup Company
Carter Hawley Hale Stores
Castle & Cooke, Inc.
Caterpillar, Inc.
Champion International
ChemicalBank
Chrysler Corporation
Citicorp
Control Data Corporation
Corning Glass Works
Dayton Hudson Corporation
Deere & Company
Dun & Bradstreet Corporation
Eaton Corp
Eli Lilly and Company
First Interstate Bank of CA
FMC Corporation
Ford Motor Company
General Motors Corporation
Gillette Company
GTE Corporation
HealthTrust, Inc.
Heinz USA
Hewlett Packard
Honeywell, Inc.
International Paper
Litton Industries
Lockheed Corporation
LTV Steel Co., Inc.
McDonnell Douglas Corporation
Merck & Company
Metropolitan Life
Montgomery Ward & Co.
Motorola Inc.
North American Philips
Ogden Allied Services
Owens Illinois
Pacific Gas & Electric Co.
Pillsbury Foods
Pitney Bowes, Inc.
Ponderosa, Inc.
PPG Industries, Inc.
Prudential Insurance Co.
Pfizer, Inc.
Raytheon Company
Shearson Lehman Hutton
Shell Oil Company
Southern Company, The
Southwestern Bell Corporation
Texaco, Inc.
Textron, Inc.
Travelers, The
TRW
Union Carbide Corporation
United Airlines
US West
USS (a division of USX Corp)
VF Corporation
Wang Laboratories, Inc.
Warner Lambert
Whirlpool Corporation
Whitman Corporation
W.R. Grace & Co.

I: COMPANY INFORMATION

Survey participants include 80 of the largest American corporations. In terms of industry they include representatives of all major non-government sectors of the U.S. economy. The jobs in these organizations are likely to be similar to many federal jobs, though no individual organization is likely to have the variety of jobs present in the federal government.

The operations of organizations participating in the survey are widely dispersed geographically, with 70% reporting multinational operations and an additional 21.9% reporting national operations. Even the 7.5% without national operations have regional operations.

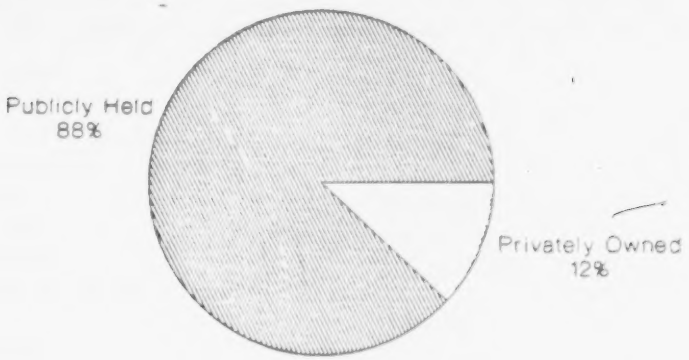
Thus, all of these organizations experience the same kinds of labor market pressures faced by the federal government, and their ways of dealing with those pressures may provide guidelines for federal government policy and practice.

I: COMPANY INFORMATION

2. Sales/revenue groups. *(N = 80)*

1.3%	Under $1 billion	15.0%	$10 to $24.9 billion
32.5%	$1 to $4.9 billion	2.5%	$25 to $50 billion
31.2%	$5 to $9.9 billion	12.5%	Over $50 billion
		5.0%	Unknown or not applicable

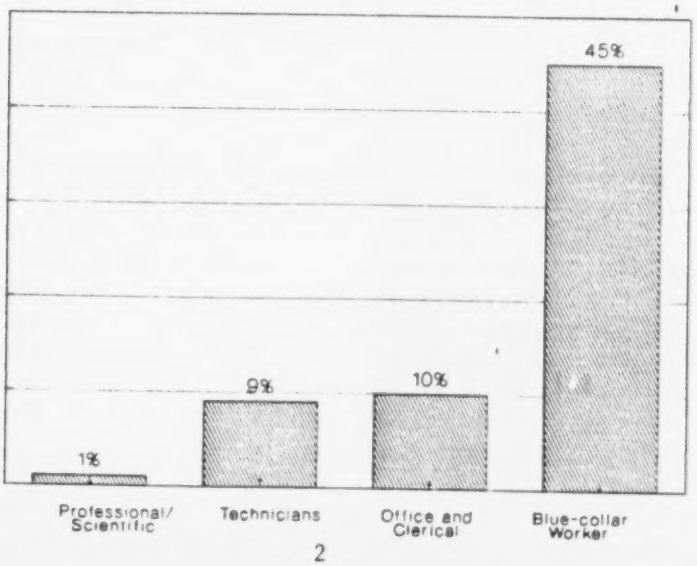
3. Ownership. *(N = 73)*



4. Total U.S. employment of participants. *(N = 80)*

24	Under 25,000	8	75,001 to 100,000
30	25,000 to 50,000	7	Over 100,000
11	50,001 to 75,000		

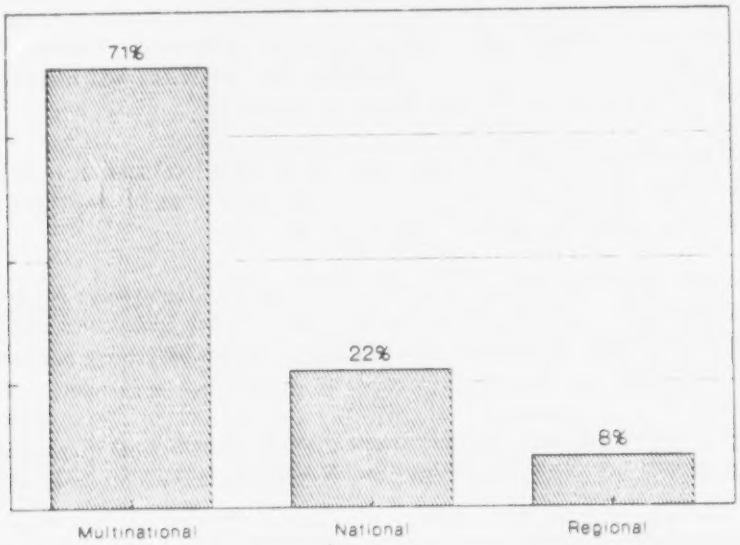
5. Percent of work force represented under collective bargaining agreements. *(N = 69)*



6. Primary Industry. *(N = 80)*

20	Durable Goods Manufacturing	10	Utilities
15	Non-Durable Goods Manufacturing	7	Services
8	Finance	7	Other Industries
9	Diversified	4	No Response

7. Geographic scope of participants' operations. *(N = 79)*



8. Number of work locations (excluding sales offices).

Mean	-	421
Median	-	100
Range	-	4 - 10,000

II: COMPENSATION STRATEGY

Sixty percent of the survey participants have a written compensation strategy/philosophy. Typically these statements refer to their competitiveness within their labor market, achieving internal equity, rewarding employees based on their performance, and/or attracting and retaining well qualified people. Most organizations use these statements for their entire corporation; over sixty percent included references of pay to local labor markets.

There are distinctly different labor markets for different occupational groups. At the executive/managerial level, over 90 percent of the respondents focus on national labor markets. National labor markets are also important for professional/scientific positions. However, for technicians and office/clerical positions, local labor markets are the primary focus for pay setting strategies.

There were mixed results as to specific strategies used for defining local and regional labor markets. Those corporations which utilize specific strategies referred to recruiting areas, areas defined by local managers, or large metropolitan area similar to MSAs.

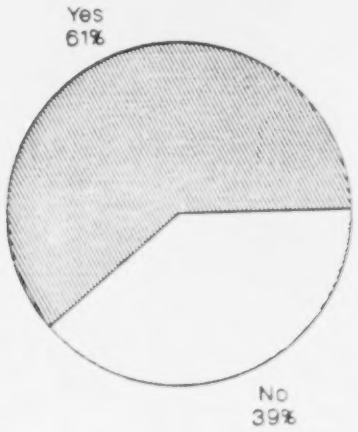
Nearly all corporations claim their average salaries are with $\pm 5\%$ of the average pay levels in their respective labor markets. Significantly, the respondents who indicated that their technicians and office/clerical workers are paid more than 10% above the market averages have collective bargaining agreements covering all or a portion of these employees.

There is a definite emphasis on market competitiveness versus internal equity for major corporations. This means that salary grades are often based more on competitive market analyses than on internal equity considerations.

It is quite clear that the overwhelming majority of these corporations do, in fact, maintain salary ranges for specific occupations based on geographic locations.

II: COMPENSATION STRATEGY

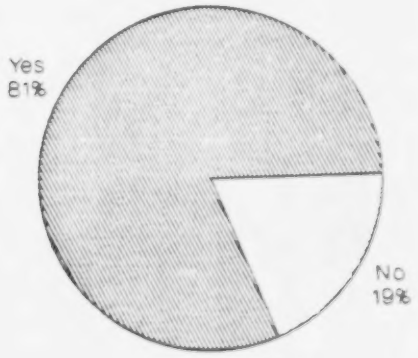
1. Written statement setting forth compensation strategy/philosophy. *(N = 79)*



If YES, typical response.

- "Pay equal to or better than community."
- "Competitive within the industry or labor market."
- "Internal equity."
- "Reward employees based on performance."
- "Attract well qualified people, encourage career building."

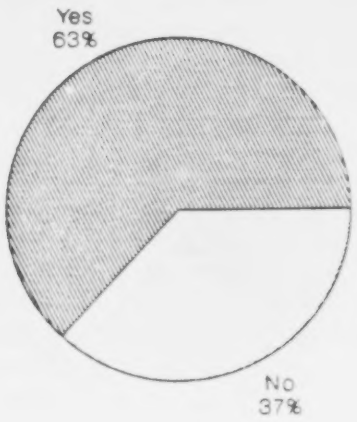
2. Written statement governing compensation program for entire corporation. *(N = 47)*



If NO, typical response.

- "Separate statements for exempt and non-exempt employees."
- "Does not cover bargaining employees."
- "U.S. domestic employees only."
- "Management only."

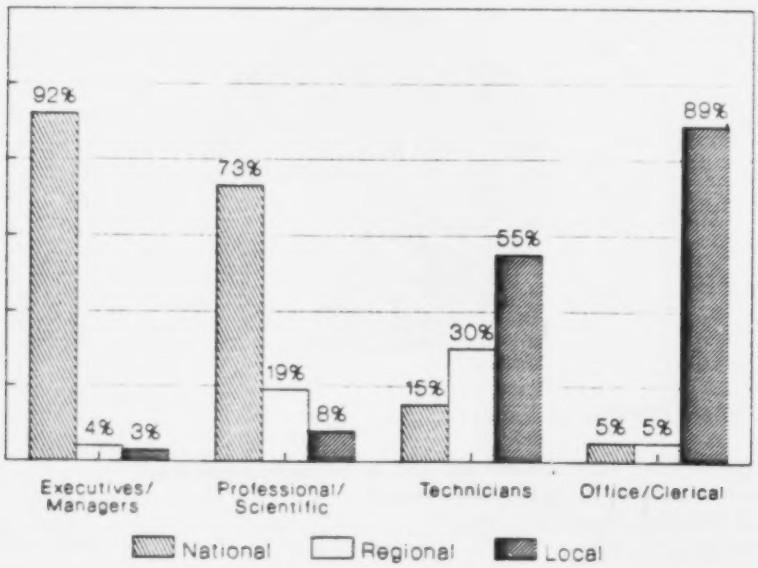
3. Statement includes a provision or reference that recognizes the concept of local/regional labor markets. *(N = 46)*



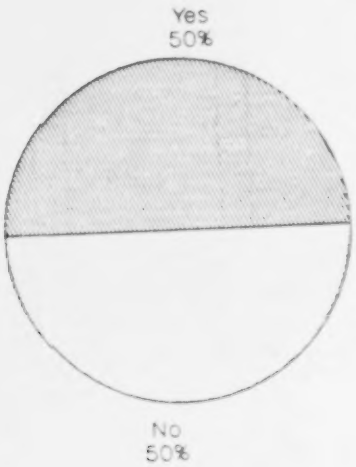
If YES, typical response.

- "Non-exempt only - pay at local competitive levels."
- "Salary ranges vary by geographic location."

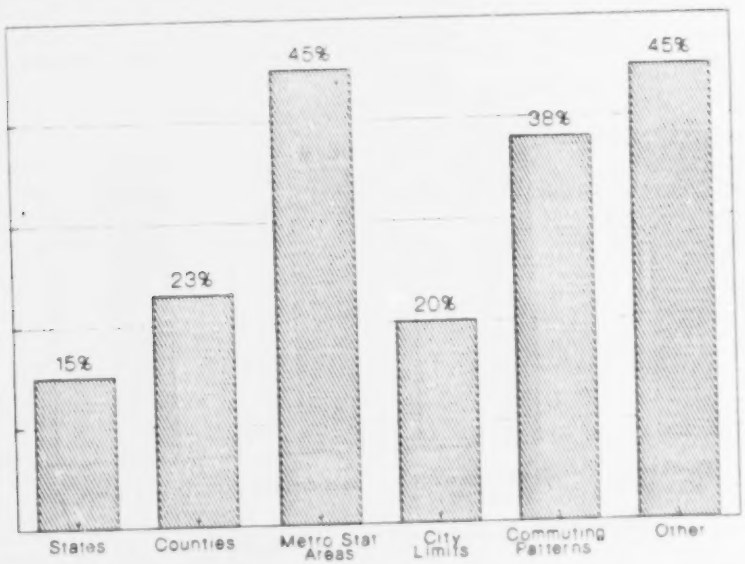
4. Primary labor market focus of pay setting strategy. *(N = 78)*



5. Specific strategy for defining geographic areas relevant to local/regional labor markets. *(N = 80)*



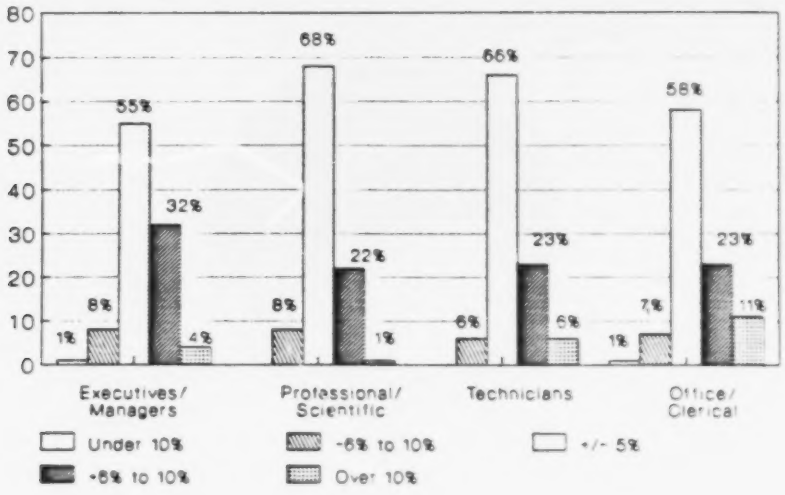
If YES, are they based on any of the following geographic areas. *(N = 40)*



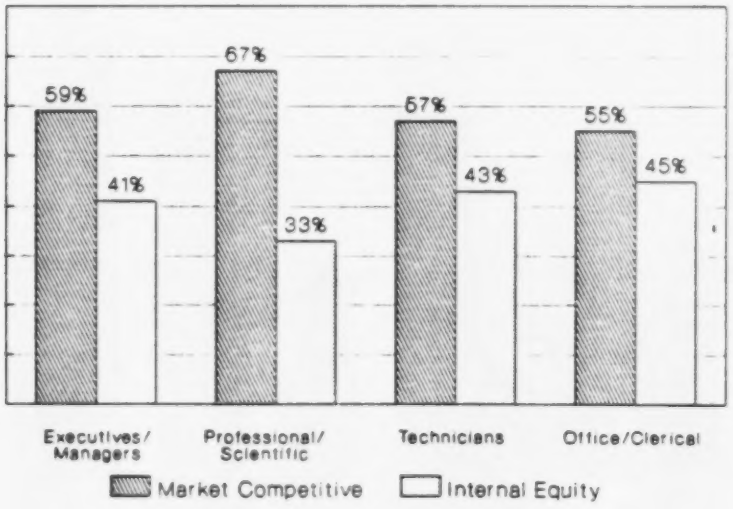
If OTHER, typical response.

- "Recruiting areas."
- "Defined by local managers."
- "Only in New York, Los Angeles, San Francisco and Alaska."
- "Large geographic areas, i.e., West Coast, New York metro."

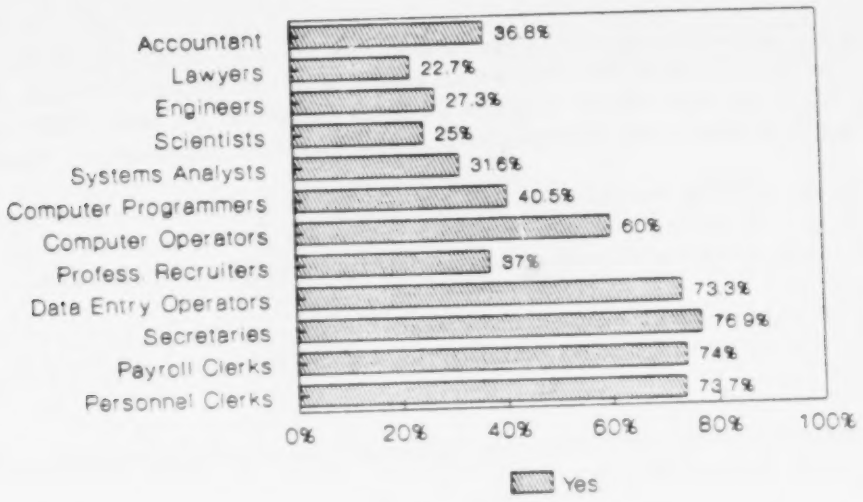
6. **Average salaries compared with competitive market averages.** *(N = 80)*



7. **Relative importance or balance in maintaining a salary program.** *(N = 76)*



8. **Different salary ranges to reflect geographic locations for identical positions.** *(N = 76)*



III: SALARY STRUCTURES

Sixty percent of the participating corporations use more than one salary structure for their exempt employees., The reasons cited for using different structures are geographic or local market differentials, subsidiaries having their own salary structures, different structures for bonus eligible and non-bonus eligible employees, use of industry specific structures, and structures for personnel on special assignment to a designated city.

Nonexempt office/clerical and technicians are not typically covered under the same salary structures as professional and other exempt positions. For those corporations with two or more nonexempt structures, the differences cited are number of grades, midpoint differentials, and local/regional market differentials.

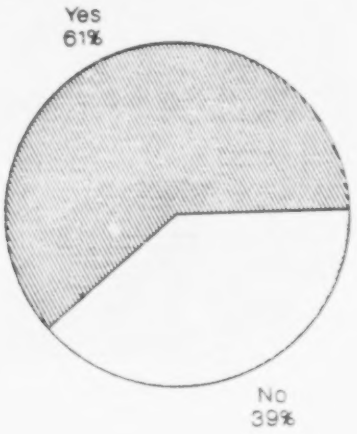
Similarly, blue collar workers are covered under separate nonexempt salary structures. Collective bargaining agreements, use of hourly rates versus annual salaries, and step progression ranges are the primary reasons cited.

A substantial majority of the survey respondents do give cash payments in addition to base salary. These are generally limited to relocation payments.

Salary range width did vary among the functional job groupings, but a majority of the corporations use between a 45% to 55% spread. Salarary range widths generally increase for higher-level positions. This is consistent with Wyatt's 1987 survey of salary management practices.
Sixty-five percent noted they have tried/tested various salary structure design concepts; the possibilities they noted include more bonus/less base, performance maximums for each range, use of skill-based pay, and wider ranges.

III: SALARY STRUCTURES

1. More than one salary structure for exempt employees. *(N = 79)*



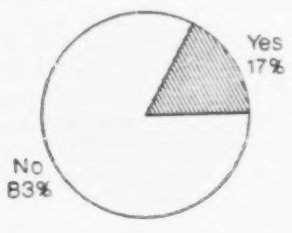
Mean	-	6.6
Median	-	4
Range	-	2 - 35

If YES, why different structures. Typical response.

- "Geographic differentials."
- "Local market differentials."
- "Subsidiaries have own structures."
- "Personnel on special assignment in Washington."
- "Bonus eligible and non-bonus eligible."
- "Industry specific structures."

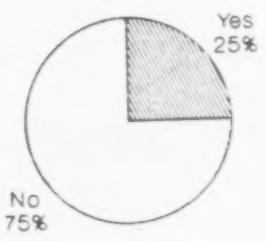
3. Non-exempt positions covered under the same salary structure(s) as professional and other exempt positions.

(N = 76)



Office/Clerical

(N = 73)

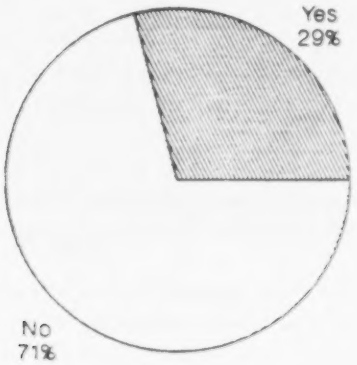


Technicians

4. How two or more non-exempt structures differ. Typical response.

- "Number of grades, midpoint differentials."
- "Local differentials."
- "Office/clerical based on city or metro area. Technicians based on regional markets."

5. Salaries/wages for blue-collar workers administered within structure used for nonexempts. *(N = 73)*

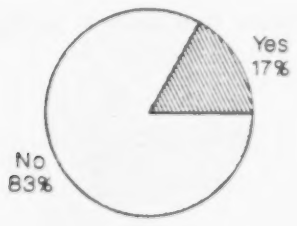


If NO, typical response.

- "Blue-collar pay is under collective bargaining agreements."
- "Hourly and salaried on different structures."
- "Blue-collar has step progression."

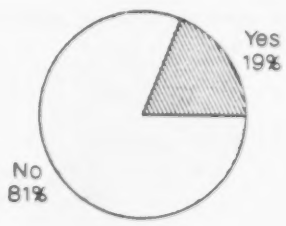
6. Assign jobs to different salary grades if using single exempt/nonexempt structure to remain competitive in different locations.

(N = 54)



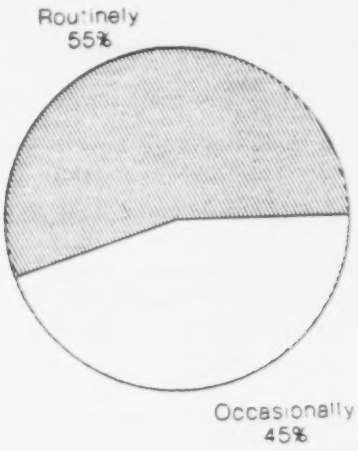
Exempt

(N = 45)

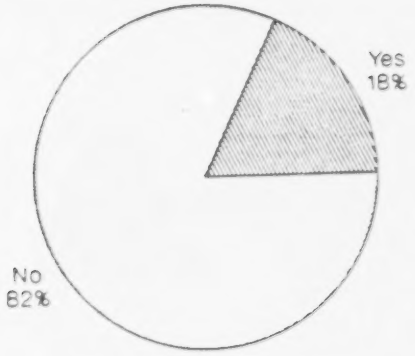


Nonexempt

If YES, how frequently does this occur. *(N = 11)*



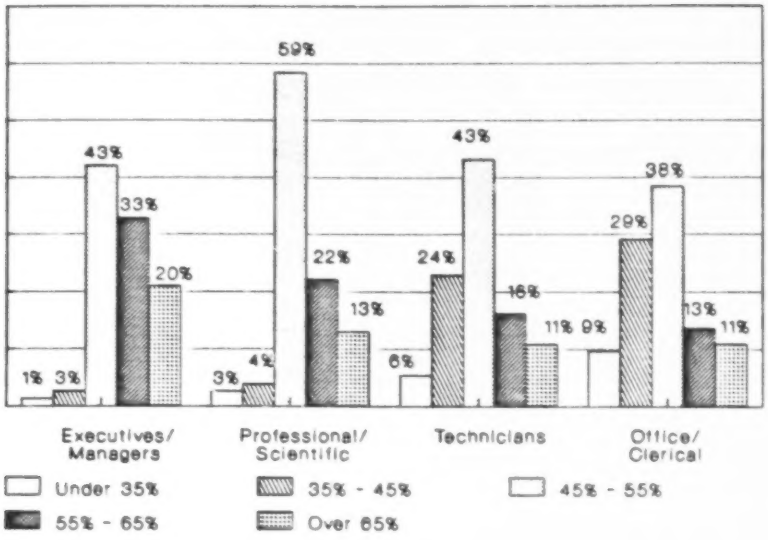
7. Cash payments in addition to base to reflect geographic differentials. *(N = 78)*



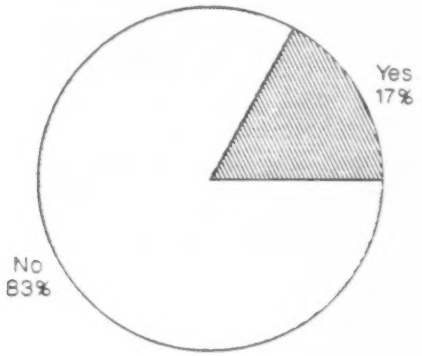
If YES, typical response.

- "Only in rare instances."
- "Only in the case of relocation."
- "Relocations to New York and Washington receive housing allowance."
- "All work locations are assigned to one of six zones, which specify differential."
- "Cash payments over three years."

8. Width of salary ranges for the following groups. *(N = 75)*



9. Tried or tested innovative structure design concepts. *(N = 63)*



If YES, typical response.

- "More bonus, less base."
- "Performance maximums within each salary range."
- "Skill-based pay."
- "Widening ranges."

IV: SALARY PROGRAM ADJUSTMENTS

Most of the participating corporations made annual adjustments to their salary structures over the past several years.

Merit pay programs are used by over 98% of the respondents covering all functional job groups. Few corporations (less than 5%) allocate annual salary increase funds to cover "general" or "cost-of-living" expenses; this concurs with Wyatts' findings in its 1987 survey on salary management practices in the private sector.

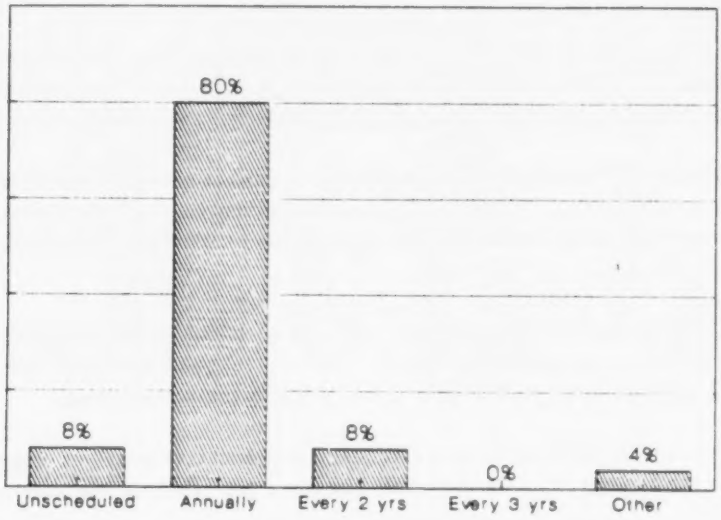
Cost-of-Living Allowance (COLA) provisions are included in current collective bargaining agreements by less than 30% of the survey participants. The COLA provisions typically cover a limited group of workers in other than white-collar positions. Only one-third of the respondents monitor cost-of-living increase rates in local areas.

The most important considerations in developing salary increase budgets for all occupational groups is the comparison of current salaries to competitive levels. This was followed closely by company or business unit profitability. The least important consideration is increases in the cost-of-living.

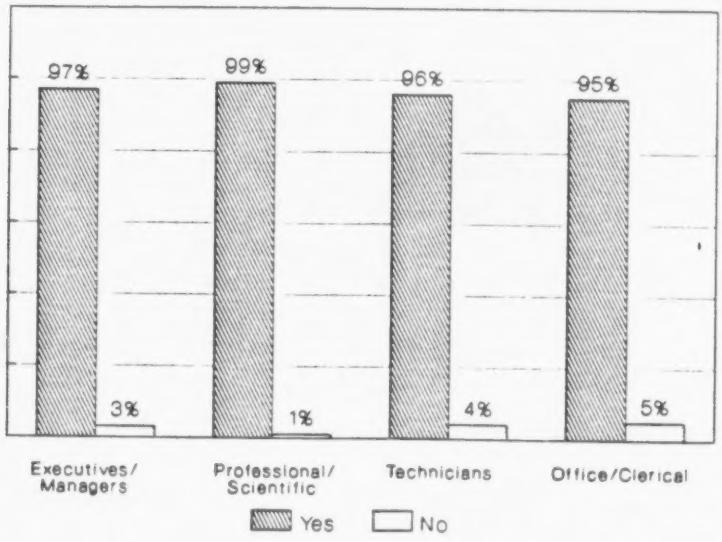
Annual incentive plans are included in the executive and managerial compensation program by virtually every respondent. Below the managerial level, however, incentives are relatively uncommon.

IV: SALARY PROGRAM ADJUSTMENTS

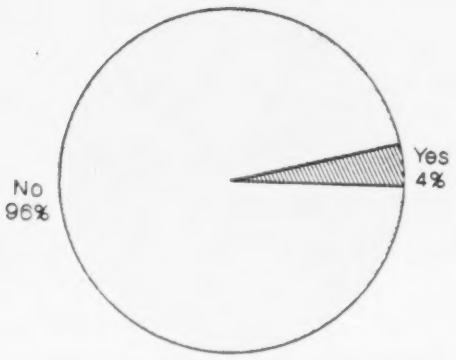
1. Frequency of salary structure adjustments over the past several years. *(N = 80)*



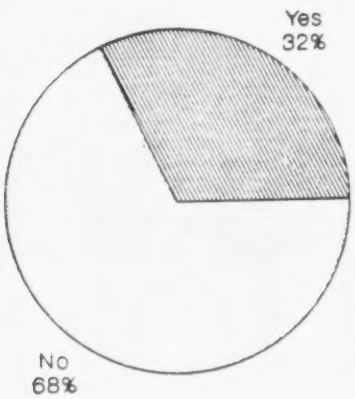
2. Formal "merit pay" program for the following groups. *(N = 80)*



3. Portion of annual salary increase for exempt employees as "general" or "cost-of-living". *(N = 80)*



4. COLA provision in current collective bargaining agreements. *(N = 71)*



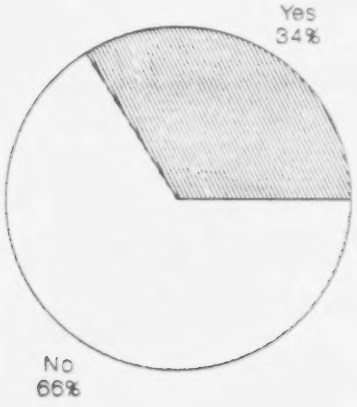
If YES, typical response.

- "All major unions."
- "Flight attendants."
- "Shop employees."
- "Mechanical and janitorial employees."

5. Most important considerations in developing salary increase budget for exempt salary program i in a typical year. Ranked by relative importance. (1=most important - 5=least important.)

	Executives/ Managers	Professionals/ Scientists	Technicians	Office/ Clerical
- Budget plans of other employers in local area	3.9	3.8	3.0	2.8
- Budget plans of other companies in same industry(s)	2.6	2.6	3.1	3.2
- Company/business unit profitability	1.9	2.0	2.1	2.1
- Comparison of current salaries relative to competition	1.9	1.9	2.0	2.0
- Increases in the cost-of-living	4.1	4.2	4.3	4.3

6. Monitor cost-of-living increase rates for region/area of facilities. *(N = 79)*



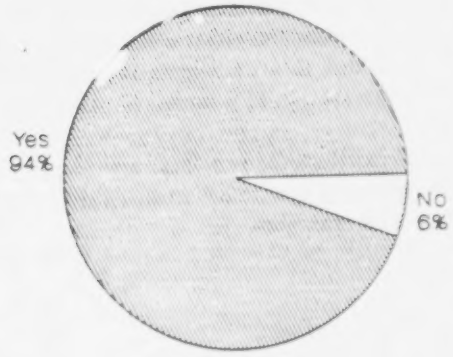
If YES, what source(s). Typical response.

- "BLS, CPI"
- "Runzheimer International"

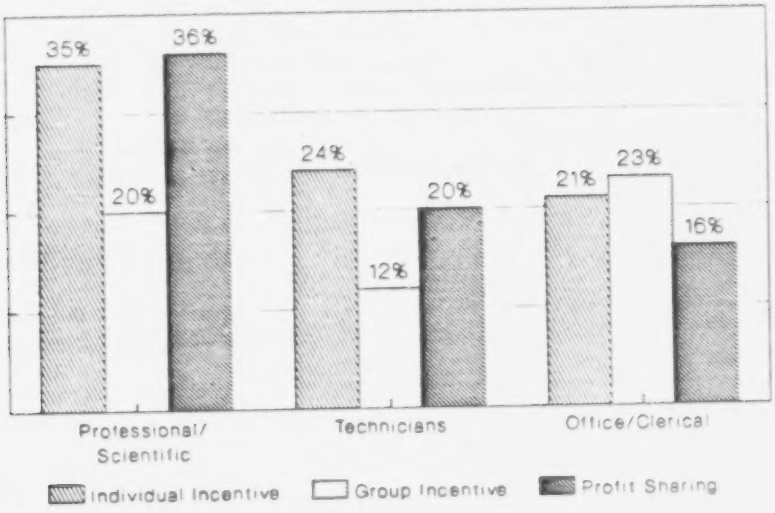
How is information used. Typical response.

- "Reference only."
- "One factor among many."
- "Used indirectly."

7. **Annual incentive plan for managers and executives.** *(N = 80)*



8. **Employee groups eligible for variable cash compensation.** *(N = 80)*



Note: Percentages are calculated as weighted averages by total employment.

V: USE OF SURVEY DATA

Salary survey data definitely serve an important function in the participating corporations' compensation programs. Seventy-five percent of the respondents either conduct or sponsor one or more salary surveys every year; a comparable percentage noted that they participate in at least 11 or more surveys per year. All participants used some variety of salary surveys as a means to plan for annual salary program adjustments.

Nearly all those organizations which conduct/sponsor local area surveys try to define their relevant labor markets. These organizations also generally seek to collect salary data at a variety of skill levels ranging from entry level jobs through executives and managers.

V: USE OF SURVEY DATA

1. Number of salary surveys company sponsors and/or conducts each year. *(N = 77)*

0	-	26 %	Mean	-	5.5
1 - 5	-	47 %	Median	-	3
6 - 10	-	16 %	Range	-	0 - 50
11 - 25	-	9 %			
Over 25	-	3 %			

2. Number of participated salary surveys conducted by other organizations. *(N = 77)*

0	-	0 %	Mean	-	34
1 - 5	-	9 %	Median	-	25
6 - 10	-	14 %	Range	-	3 - 150
11 - 25	-	34 %			
Over 25	-	43 %			

3. Salary surveys used to plan annual salary program adjustments. *(N = 80)*

41% - Government surveys.
- 39% - Area Wage Surveys
- 23% - Industry Wage Surveys
- 23% - National Survey of Professional, Administrative, Technical and Clerical Pay (PATC Survey)

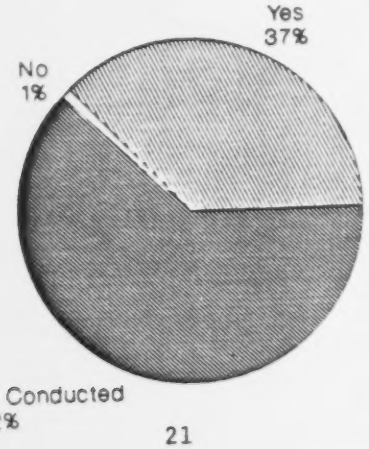
64% - We conduct our own surveys.

83% - Industry or professional association surveys.

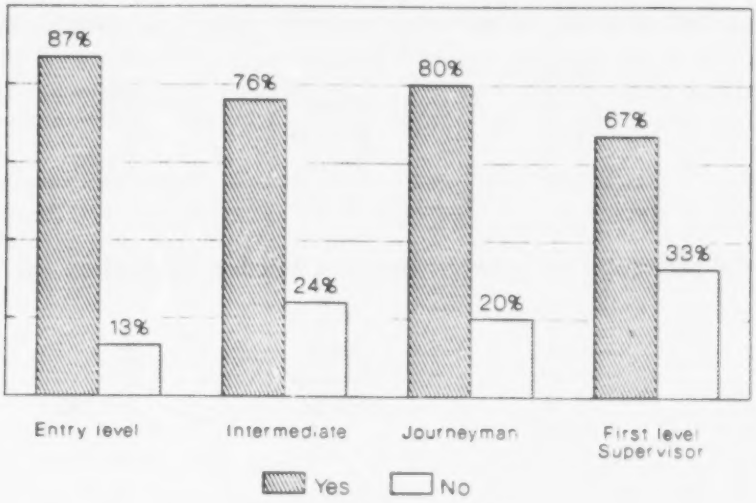
If OTHER, typical response.

- "Consultant run surveys."
- "Personnel association surveys."

4. Defines relevant labor market when conducting or sponsoring local area surveys. *(N = 73)*



5. Collects data for various skill levels if conducting own surveys. *(N = 46)*



If ADDITIONAL LEVELS, typical response.

- "Executives/managers."
- "Top of career path."
- "Second and third level managers."

VI: RELOCATION POLICIES

Ninety-three percent of respondent corporations indicated they have written policies governing employee relocation. In general, most participants cover all company-initiated relocations. Managers paid less than $75,000 and professionals paid less than $50,000 are the two most frequently relocated employee groups. Almost all direct expenses from moving household possessions to closing costs are paid or reimbursed. The majority of respondents provide a mortgage differential and arrange on some basis to protect the employee from possible problems on the sale of his/her residence. The respondents either (or both) agree to purchase the home or establish a loss protection arrangement. The majority also gross-up the employee's income to cover the tax on nondeductibleamounts.

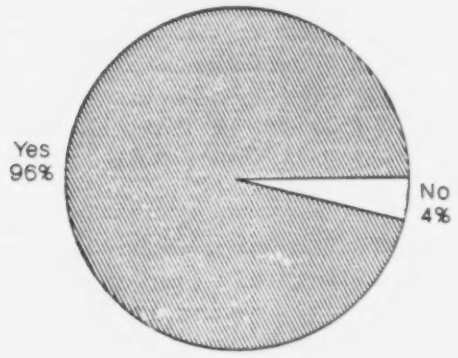
Less than 20% of the respondents have policies requiring relocated employees to pay back any portion of the reimbursed amounts if they terminate within a specified period, such as one year.
When employees are relocated from a low to high cost area, special financial arrangements such as mortgage interest differentials, increases to base salary, or lump sum payments based on cost-of-living indices are given by 60% of the survey participants. Moving from a high to low cost area usually does not affect the relocation package.

The primary sources for determining cost-of-living differentials are Runzheimer International, Economic Research Institute and CPI data.

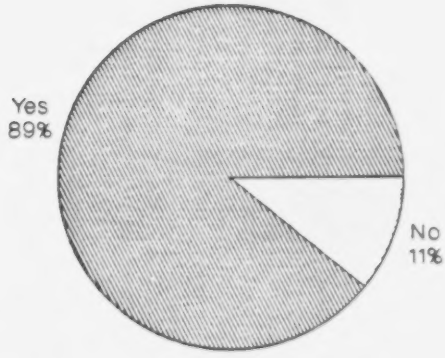
Eighty-five percent of all employee relocations involve promotions. The median average promotional increase is 10%; the median maximum promotional increase is 15%.

VI. RELOCATION POLICIES

1. Written policy for governing relocation of employees. *(N = 76)*



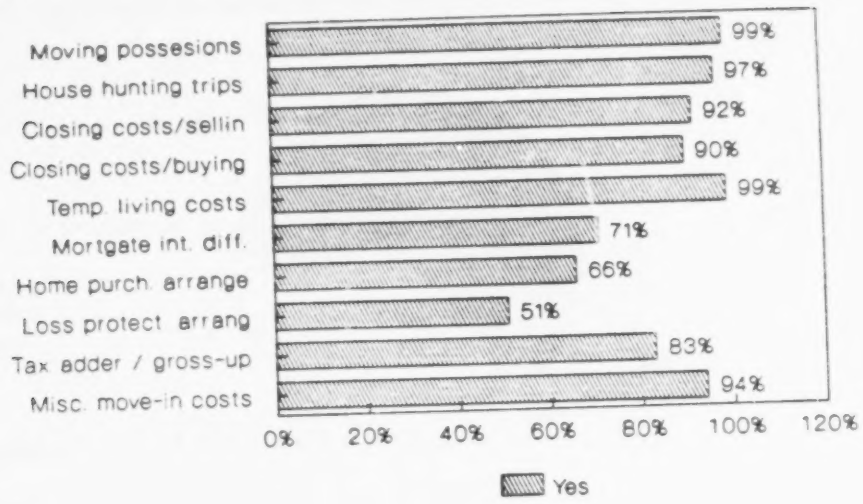
If YES, are all employee relocations initiated by the company and covered (excluding senior executives). *(N = 76)*



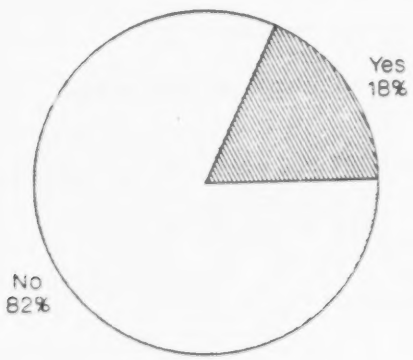
3. Percentage of relocated employees. *(N = 48)*

16.3%	-	Managers paid more than $75,000
38.8%	-	Managers paid less than $75,000
17.7%	-	Professionals paid more than $50,000
25.6%	-	Professional paid less than $50,000
1.4%	-	Technicians
0.6%	-	Office/Clerical

4. **Company paid/reimbursed items under relocation policy.** *(N = 80)*



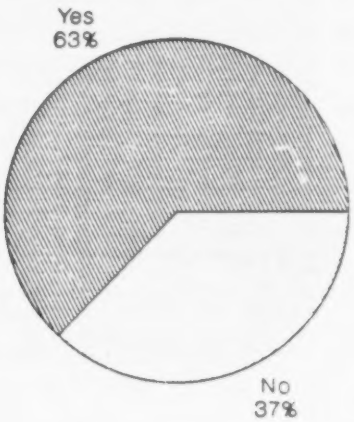
5. Specified period for employment when job change is covered by relocation policy. *(N = 78)*



If YES, requirement and/or consequence of early termination. Typical response.

- "Reimbursement if termination within one year."

6. Special financial arrangement when moved from low cost to high cost area. *(N = 76)*



If YES, describe practice and how amounts are determined.
Typical response.

- "Mortgage interest differential."
- "Discretionary percent of salary."
- "Larger increase in base salary if moved to high cost area."
- "Lump sum cash payment based on COL."
- "Percent of salary for 3 years."
- "Difference in mortgage principal and interest for 2 years."

7. How relocation package is affected when employee moves from high to low cost area.
Typical response.

- "No change in package."
- "Generally does not."
- "No relocation differential."

8. Source(s) used as information for comparing living costs between locations.
Typical response.

- "Runzheimer data"
- "Economic Research Institute"
- "BLS"

9. Other cash payments to relocated employees not linked to documented expenses.
Typical response.

- "One month lump sum payment."
- "Discretionary lump sum payment."
- "10% of salary."
- "$3,500 allowance."

10. Percentage of employee relocations involving promotions. *(N = 61)*

Mean	-	74
Median	-	85
Range	-	10 - 98

Average promotional increase. *(N = 61)*

Mean	-	11
Median	-	10
Range	-	3 - 20

Maximum promotional increase. *(N = 44)*

Mean	-	16
Median	-	15
Range	-	7 - 30

Relationship between promotional increases and other special payments when promoted. Typical response.

- "Separate issues."
- "No relationship."

VII: PROGRAM ADMINISTRATION

More than half of the participants have a program based on a uniform compensation strategy with decentralized administration; 24% have a uniform compensation strategy but manage it from a central office; and 22% give their business units the responsibility for developing and maintaining their own compensation programs.

Less than 40 percent of the respondents rely on the parent company staff to evaluate (i.e., determine appropriate salary grades) for all white-collar jobs. In the other respondents, the parent company staff has responsibility for a limited group of positions (e.g., all executive and headquarters positions) or for auditing evaluation decisions made by other personnel specialists.

Consequently, 38% of the respondents indicated two comparable white collar jobs might not be assigned the same salary range. The primary reasons cited were geographic/locality pay (72%) and industry pay differentials (47%). This is a confirmation of the results from our 1987 survey of Salary Management Practices.

In the majority of the surveyed corporations, most parent companies must approve their business units' exempt salary structures; this also holds true for nonexempt salary structures.

Responsibility for individual salary actions, however, is normally delegated to local personnel managers or business unit heads. Individual merit increases are typically approved by the business unit head while he/she shares responsibility for deciding starting salaries. Personnel managers generally retain responsibility for approving salary grade changes. Significantly, the employee's immediate supervisors are responsible for salary actions in less than 20% of the responding corporations.

Typically, the salary action decisions are made within policy limitations established by the personnel function and approved by senior management. Personnel policies, and specifically, salary adjustment budgets, are reviewed each year by a centralized staff; operational decisions then are often delegated to local managers.

VII: PROGRAM ADMINISTRATION

1. Best description of approach to salary administration. *(N = 78)*

   24% Program is based on a uniform compensation strategy, with centralized administration.
   54% Program is based on a uniform compensation strategy, with decentralized administration.
   22% Business units are responsible for developing and administering their own salary programs.

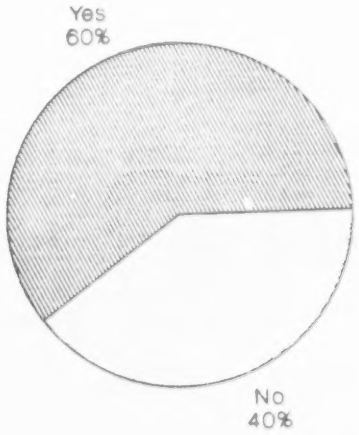
2. Role of parent company staff in evaluation of white collar jobs. *(N = 79)*

   36.7% The parent company staff is responsible for evaluating all white collar jobs.
   43.0% The staff is responsible for evaluating all headquarters jobs and executive/managerial jobs throughout the company.
   10.1% The staff is responsible for evaluating all headquarters jobs and all exempt jobs throughout the company. Nonexempt jobs are evaluated locally.
   25.3% The staff regularly monitors or audits the job evaluation process used in the business units.
   43.0% The staff is available to serve in a consulting role for the business units and in this capacity occasionally studies business unit programs.
   3.8% The parent company staff has no involvement in business unit job evaluation decisions.

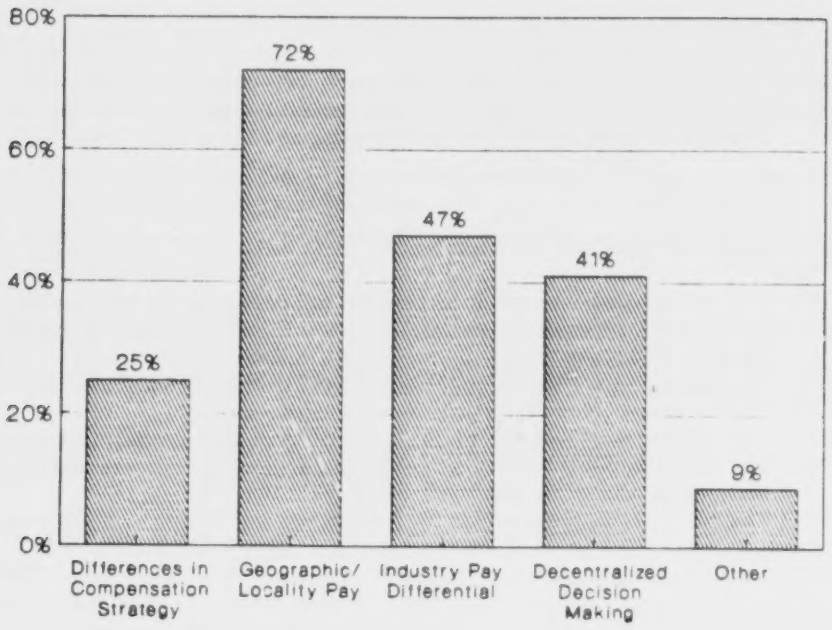
   If OTHER, describe the staff's responsibility. Typical response.

   - "Executive level jobs."
   - "All headquarter's jobs."

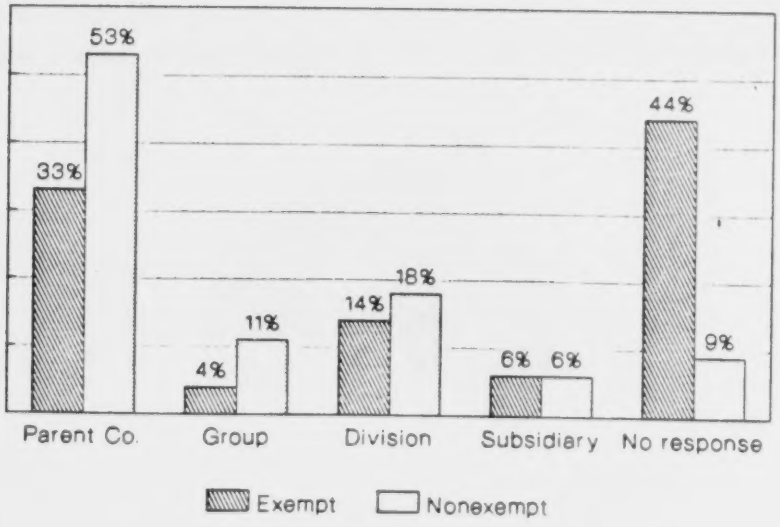
3. Two comparable white-collar jobs in same occupational group be assigned same salary range. *(N = 78)*



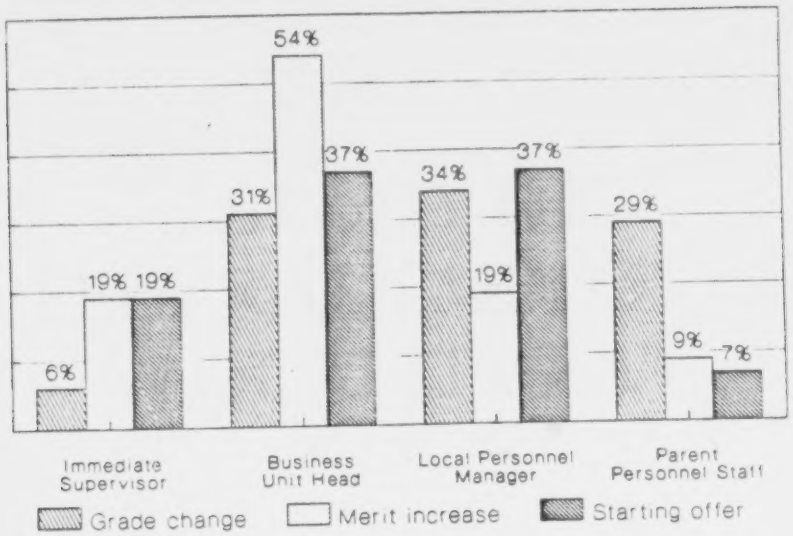
If NO, reasons that would account for differences.



4. **Organizational level exempt and nonexempt salary structures are approved.** *(N = 50)*



5. **Final approval authority for salary actions.** *(N = 70)*



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STUDY OF FEDERAL EMPLOYEE LOCALITY PAY

TASK 3: *Comparing Private vs. Federal Pay On A Local Basis*

TASK 3 - COMPARING PRIVATE VS. FEDERAL PAY ON A LOCAL BASIS

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APPENDIX 36

APPROACH TO THIS TASK

The analyses for this Task are based on a database of salary survey information assembled by the Office of Personnel Management. The database includes data from three national survey organizations:

- Bureau of Labor Statistics (BLS);
- Executive Compensation Service (ECS), a subsidiary of The Wyatt Company; and
- Mercer Meidinger Hansen.

In combination, the database is one of the largest ever compiled. The surveys that were used are listed, by title, in the Appendix.

Survey sources report summary data--means and medians[1]--for a series of "benchmark" positions. These are generic positions defined with brief descriptions of typical duties. The benchmark position concept has been used in surveys for over 30 years. The objective is to "match" the benchmark positions to actual positions found in the organizations participating in the survey. For use in this study, the OPM classification specialists matched the survey benchmarks to federal positions, specified by series and GS grade level.

Although the survey sources are not disclosed in the database, the reported means and medians represent the combined results from several sources.

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[1]Mean and median values are both measures of central tendency, and often used interchangeably as "average" values. A mean is calculated by adding the reported salary values and dividing the sum by the number of observations or, in this context, job incumbents in the benchmark positions. A median is determined by arraying the individual survey data from high to low, and identifying the value in the middle, the 50th percentile. With a symmetrical, "bell shaped" distribution, the mean and median, are equal. Salary survey data generally do not form a symmetrical distribution; typically, there are a disproportionate percentage of low values. Where this is the case, the mean will exceed the median, and the median is often used to describe the data. This is true, for example, in discussions of average income levels across the United States, where a small number of extremely high income levels tend to raise the means but have little, if any, effect on the median values.

A comprehensive listing of the federal series for which survey data are reported is included as an Appendix.

In addition, where adequate benchmark job data are not available, the database includes "constructed" data extracted from the report, Geographic Salary Differentials, published by the consulting firm, Mercer Meidinger Hansen. This report and the underlying analytical methodology are based on a compilation of data from a variety of published surveys. As the basis for the survey report, national average pay rates are determined for each benchmark job and compared with reported local rates. The differences between the national and local averages, across the several survey sources, provide the data for linear regression analyses for each metropolitan area and the resulting regression equation makes it possible to estimate the local pay level at any specified national salary. Using equations from two or more local areas makes it possible to use the survey averages from one area (assuming it is one for which equations are provided) to estimate the comparative market pay levels in another local area. In effect, the equations provide a basis for inferring local salary levels where actual survey data are not available.

While the Mercer Meidinger Hansen results are based on actual survey data, the equations are intended for use in comparing general pay levels in one area with pay levels in other areas. The equations have been used by OPM to infer local pay levels for specific benchmark jobs, in the absence of actual data, but cannot be interpreted as valid measures of what a benchmark job would or should be paid. (While individual job estimates cannot be used in the same way as actual data, OPM analyses show that there is generally a high correlation between the constructed data and actual data for local areas where both exist.) Accordingly, we have relied on the constructed data to provide aggregate estimates of the differences between federal and private sector pay levels.

The analyses included in this report are based on actual survey data, unless specifically attributed to the constructed data. All results relevant to specific benchmark jobs are based on actual survey data.

From our perspective, the analytical results and conclusions based on both the actual and constructed survey data should be useful for the intended research purpose, but will need to be confirmed with supplemental surveys. We anticipate that new surveys and the replication of our analyses will confirm and refine our results.

All survey results are reported by Metropolitan Statistical Areas (MSA's). These areas are defined as a large metropolitan area, and selected contiguous counties. The Washington, D.C. MSA, for example, is defined as the District of Columbia plus Loudoun, Fairfax, Arlington, Prince William and Stafford counties and the incorporated cities within these counties in Virginia, and Charles, Prince George's, Montgomery, Calvert and Frederick counties in Maryland. Actual survey data are reported for 26 MSA's which are listed in Exhibit I. Constructed survey data are reported for an additional 22 MSA's.

A total of 768,134 federal white-collar employees are represented in the database for these MSA's, or approximately 55 percent of the work force covered under the GS program.

Exhibit I

METROPOLITAN AREAS
WITH ACTUAL SURVEY DATA

Metropolitan Statistical Area	Federal Employees
Atlanta	18,506
Baltimore	29,710
Boston	13,593
Chicago	18,067
Cincinnati	4,484
Cleveland	6,746
Columbus	5,346
Dayton-Springfield	16,296
Denver-Boulder	17,315
Detroit	11,362
Fort.Worth-Dallas	14,206
Houston	8,144
Indianapolis	8,109
Kansas City	14,061
Los Angeles	21,719
Minneapolis-St. Paul	4,876
Nassau-Suffolk	5,694
New York	20,992
Philadelphia	32,683
Phoenix	4,378
Richmond-Petersburg	6,125
St. Louis	18,597
San Diego	14,885
San Francisco-Oakland	23,503
Seattle	7,281
Washington, DC	221,166
Total	567,844

WYATT'S COMMENTS ON THE VALIDITY OF THE SURVEY DATA

Salary surveys are almost always based on samples and, as such, are subject to the same sample design considerations as, for example, public opinion surveys. With salary surveys, the objective is to determine the level of pay for supposedly comparable positions across a defined population of employers. Generally, the relevant employers are limited to an industry, a geographic area, or size range (typically based on revenues or number of employees). In some surveys, specific employers are selected from the overall population, based on predetermined criteria so that the resulting sample is statistically representative of the population. The assumption is that the salary data collected from the sample will be a valid "snapshot" of rates of pay across the overall population. Realistically, only the Bureau of Labor Statistics conducts broad-based surveys that are intended to be valid, cross-sectional surveys.

Although industry groups and consulting firms conduct surveys that involve meetings and other personal contacts to encourage participation by an adequate group of pre-selected employers, the cost of these surveys is high (due to the time required both for planning and for conducting the meetings involved in data collection), and only a limited number of employers is willing to sponsor them.

Consequently, most salary surveys are based on a mass mailing of questionnaires to a list of employers, with little, if any, prior screening. There may be a follow-up contact, either by telephone or mail, to encourage participation, but this depends on the number of questionnaires distributed and the willingness of the survey sponsor to invest the additional time. The survey questionnaires are usually completed by a personnel specialist on the staff of the participating organization.

These surveys hardly meet the standards to be considered a valid sample. There has been virtually no research to determine whether this approach introduces a consistent bias, and the absence of research is presumably indicative of the

minimal concern among survey users. Every survey produces somewhat different results, and most employers use multiple surveys, often averaging the differences.

Some surveys are certainly considered to be better than others. Quality is affected both by the design of the survey questionnaire and by the level of effort to review and "clean up" completed questionnaires.

In fact, the OPM staff placed a heavy emphasis on survey quality in selecting sources for the database. A number of alternative national sources were evaluated and rejected. While the database is not as extensive or as valid as the BLS will need to develop in order to meet our recommended program requirements, this database is , in our opinion, the best that can be developed from existing data.

On a related point, we want to state our concern about a specific data quality issue--the job matching process. Job matching is a fundamental issue in conducting and using survey data. While the BLS staff makes this a basic question in the data collection phase of its surveys, in other national surveys the process is typically completed by a lower-level personnel specialist in each participating employer. It is reasonable to assume that their matches are not completely valid, although there is no evidence to indicate the magnitude or the direction (i.e., the job matches over- or under-state prevailing pay levels) of the problem. For the same reason, the use and interpretation of survey data is dependent on valid job matching.

While we have no reason to distrust the job matches established by the OPM classifiers, we are concerned about the matches from two perspectives. First, there is the question of data validity. Valid data in this context would be defined as accurate measures of the mean salaries paid for workers performing jobs that are, in fact, comparable to the benchmark jobs. OPM has no control over this issue, and we have to assume that errors in data collection are random and that, in the combined database, individual errors are offsetting.

Our second concern relates to the necessary assumptions about the nature and level of work done, across government, at each GS level. The OPM staff has to assume that the work done at each GS level is consistent with the definitions established by title 5 U.S.C. There is, of course, a recognized problem of overgrading (e.g., jobs at GS-6 that should properly be assigned to GS-5), and erroneous assumptions about job matches would significantly overstate the difference between federal and private sector pay levels. For clerical and technical occupations, the difference between benchmark levels is typically 10 to 15 percent. For professional and administrative occupations, the differences are generally 15 to 25 percent. In matching to benchmark jobs, a common mistake would be to exaggerate the internal job and to match it with a higher survey job, thereby overstating the market pay level. A similar result occurs when jobs are assigned to higher salary grades than is justified by actual job content. (This is the overgrading situation.) It is also a problem if the matching understates the market level. This has the potential to be a serious problem that wa ants further study.[2]

Assuming that the survey data are sufficiently valid and that the OPM job matches are also sufficiently valid for research purposes, the means and medians are defensible measures of private sector pay. However, since the surveys were independently conducted and only summary results reported, there is no basis for looking at the variance (or distribution) of pay levels around the means. This makes it impossible to consider either percentile values or standard deviations.

Despite these comments, we are comfortable with the database as the basis for this study. OPM has relied on the best of the existing national surveys. The combined surveys represent the best database that can be assembled, and for the

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[2]For example, the mean salary for a federal GS-8 secretary is $24,869 and in the database this position is matched with a private sector secretarial position paid $29,179, a 17.3% difference. However, if the actual duties performed by the typical federal secretary at GS-8 are more comparable to the next lower level of private sector secretary, the pay comparison is: the federal mean, $24,869 vs. the private sector mean, $24,592. This is not to suggest that this specific match is invalid, but rather to illustrate that the "internal matching" is as important as the external ranking.

research purpose of this study is fully adequate. We are recommending that BLS be responsible for any future surveys used in the white-collar salary program. Their expertise in designing and conducting salary surveys should result in a better database than is available at this time.

As the saying goes, salary management is "more of an art, than a science." There are very few private sector organizations that share the government's concerns about survey data validity. Private sector employers do not generally use survey results in a mechanistic manner such as that applied to PATC data. Rather, the results are considered as one of a number of factors in making what is basically a policy decision to adjust the salary structure. Moreover, few employers have multiple locations with more than a small staff. Thus, the cost implications of invalid data are not an important issue. Finally, if a private employer experiences recruiting or retention difficulties which are attributed to pay, the salary program can generally be adjusted quickly to be more competitive. There are few situations that would warrant the additional cost to sponsor or conduct a survey based on a statistically-valid methodology.

LABOR MARKETS AND THE USE OF SURVEY DATA

Survey data are compiled to help employers study prevailing pay levels in the labor markets relevant to their work force. To use survey data properly, it is fundamentally important to understand the labor markets in terms of the geographic boundaries (i.e., the areas considered in developing recruiting plans), and/or product or service markets (for specific knowledge and skills). In reality, each occupation and probably each job level has a unique labor market since an adequate supply of labor with the requisite skills typically lives in an irregular and continuously shifting pattern around a work site. As a rule, positions requiring higher level knowledge or skills necessitate recruiting in an increasingly larger labor market.

For clerical, technical and hourly jobs, the relevant labor market is generally considered to be "local" since most prospective applicants live within a relatively short distance of the work location. The labor markets depend on available commutation alternatives and other comparable job opportunities. Rivers and other commutation barriers often serve as labor market boundaries. In many metropolitan areas workers may be unwilling to commute more than a few miles, while in more rural areas, where jobs are less plentiful, normal commutes are often longer.

It is possible to determine relevant labor markets from personnel records, but, realistically, this is time-consuming and probably unnecessary. It would, of course, be possible to plan and conduct a survey that is statistically valid for a specified labor market. However, most employers participate in or purchase more loosely designed surveys that include data for workers in a broader labor market.

Wyatt's survey subsidiary, Executive Compensation Services (ECS), produces two survey reports that provide data for Clerical and Technical series positions. These surveys report data for MSA's, consolidated MSA's (a somewhat larger geographic area), states and multi-state regions. Neither survey reports "national"

results. This reporting format is indicative of the use of the data and the general understanding of the labor markets for these occupations.

Moving into the Professional and Administrative series, the labor markets generally become larger. Although in a few major urban areas, such as New York and Los Angeles, the market is still predominantly local, most of the recruiting and executive search activity is planned around increasingly larger regional areas as job openings occur at higher steps on the occupational career ladders. For managerial, executive, and the highest professional level jobs, the labor markets are best described as national with the actual scope of a job search dictated by the locations of the nation's more prominent corporations.

The problem in defining these labor markets is that while it is realistic to assume that MSA's are too small, there are no consistent regional areas that can be delineated as distinct labor markets. For example, Richmond and Norfolk, Virginia evidence significantly different salary levels than does Washington, D.C. The Commonwealth of Virginia recognized this situation with salary differentials for employees based in the Washington, D.C. suburbs. Similarly, it would be a mistake to pay professionals or administrators in Albany, Rochester and Buffalo, New York, the same as those based in New York City. These cities cannot be considered as part of the same labor market.

Our experience suggests that there are differences in pay levels between urban and rural areas, but the OPM database does not include data for areas outside of the MSA's. If this is true, it may reflect the concentration of large corporations in urban areas. Since a significant percentage of the government's professionals and administrators work outside of the major urban areas, it would be useful for the BLS to study this in future surveys. From our perspective, it would be difficult for the government to justify pay differentials for this group of non-urban employees unless the pay differences are consistent and significant.

In the absence of readily identifiable regions, we recommend that the government continue to define the labor market for professionals and administrators as national, but to exclude the few high pay metropolitan areas in the calculations to determine national norms. The survey database suggests that pay levels for these occupations in Los Angeles, San Francisco and New York and its environs are significantly above the prevailing pay levels across the balance of the nation. The survey data for other urban areas do not evidence significant differentials which leads us to conclude that the same salary schedule with perhaps a few other exceptions can be used across the country. Each clerical and technical schedule will be based on local pay levels.

There is a need for the BLS to confirm these tentative conclusions. While we are comfortable with the database for research purposes and initial policy action, it is not adequate for final policy decisions and may require supplemental information.

If the limited number of high pay areas is confirmed, these areas warrant, and at least in some instances almost demand, special salary differentials. These areas are often treated differently under corporate policies, and recognized as difficult locations for recruiting. Higher pay levels (in the form of separate salary differentials) along with relocation assistance is fully justified. Our recommendations on these issues are discussed in the Task 4 report.

It will be important to exclude the high pay areas in the calculations and the interpretation of survey data for the balance of the country. Including data for these areas will effectively raise the result for other areas, thus, resulting in overpayment. This is, of course, part of the current problem.

For all practical purposes, the labor markets for Clerical and Technical employees are independent of those for Professional and Administrative employees. There are some "gray area" occupations and job levels, but the independence of

these two groups is reflected in the personnel policies and practices of virtually every employer. Some of the differences in policies are undoubtedly attributable to the exempt/nonexempt distinctions. However, the overriding difference reflects the dynamics of the labor markets as reflected in corporate recruiting and staffing strategies. It is impractical and expensive to ignore the realities of labor markets.

ANALYSES AND CONCLUSIONS

The database is well suited to a variety of analyses. Each MSA has to be analyzed independently, but there is also a need to compare the MSA results. Overall, the objective is to understand the differences across labor markets.

It is important to emphasize that the actual survey data are generally available for the larger cities. The constructed data are provided for smaller cities. There is a pattern that shows higher salary levels in the larger cities, although there are several prominent exceptions. Since we have elected to limit our job-to-job comparisons to the actual survey data, the results may appear to overstate the differences between federal and private sector pay levels. When adequate survey data are available for the smaller MSA's, it may reduce the apparent gap. (The actual gap will not be affected by collecting additional survey data for new cities since the factual situation is unchanged.)

- The Pay "Gap": An Overview

The four maps, Exhibits II through V, summarize the comparison of federal salaries with private sector salaries in the 48 MSA's. Each map shows the comparative results for a broad PATCO occupational category: Professional, Administrative, Technical, Clerical and Other series. (The comparison is based on constructed data where actual data are unavailable.)

We note the following:

- there are no distinctive or consistent regional patterns;
- metropolitan areas that are low for one occupational group tend to be low for the other three, but the pattern is not consistent;
- the largest metropolitan areas tend to have the highest overall salary levels, but, for the Technical jobs, there are pockets of high pay in unexpected locations; and
- there are relatively few areas where private sector salaries are lower than federal salaries.

PROFESSIONAL POSITIONS

PRIVATE SECTOR PAY RELATIVE TO FEDERAL PAY

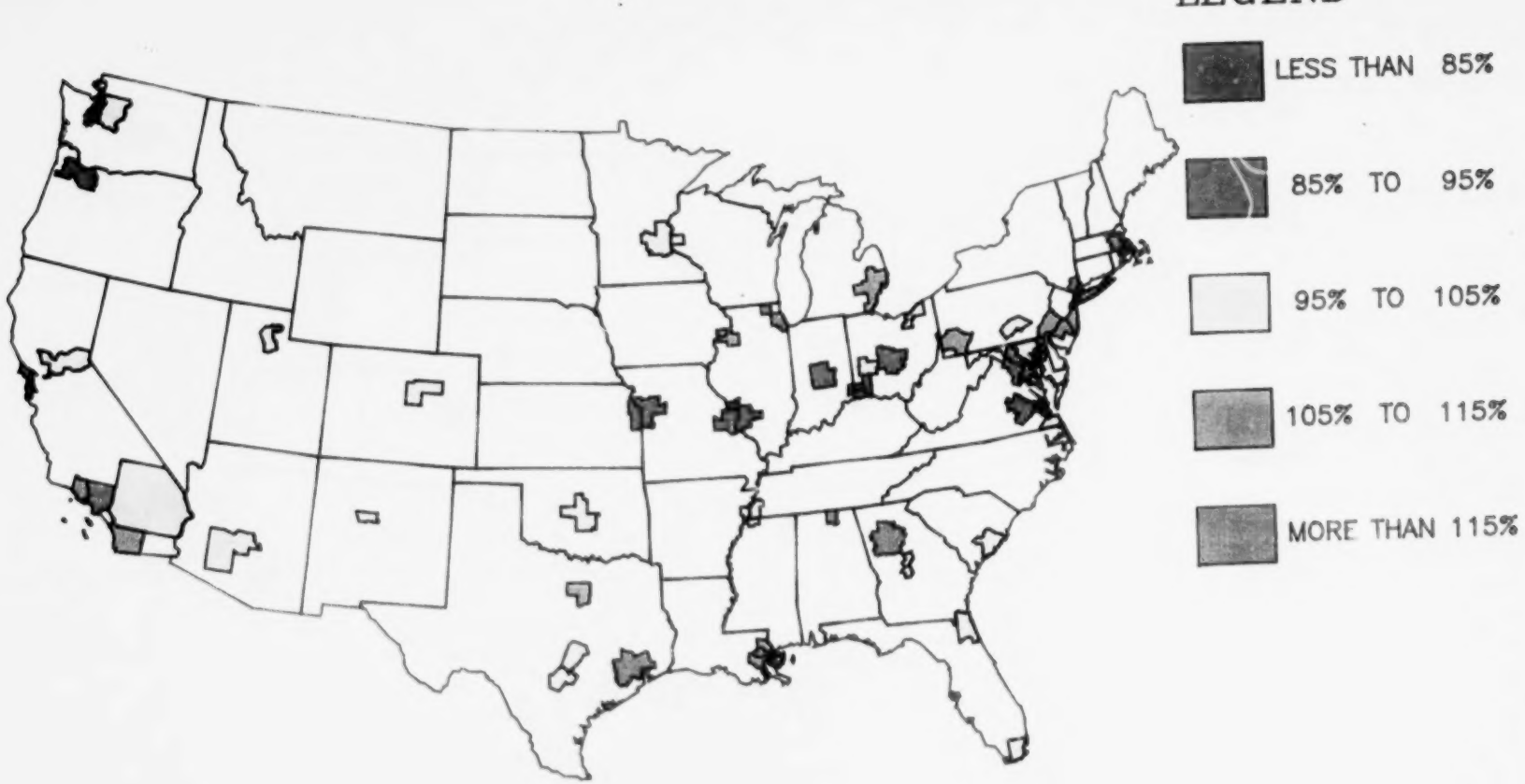

Exhibit II

ADMINISTRATIVE POSITIONS

PRIVATE SECTOR PAY RELATIVE TO FEDERAL PAY

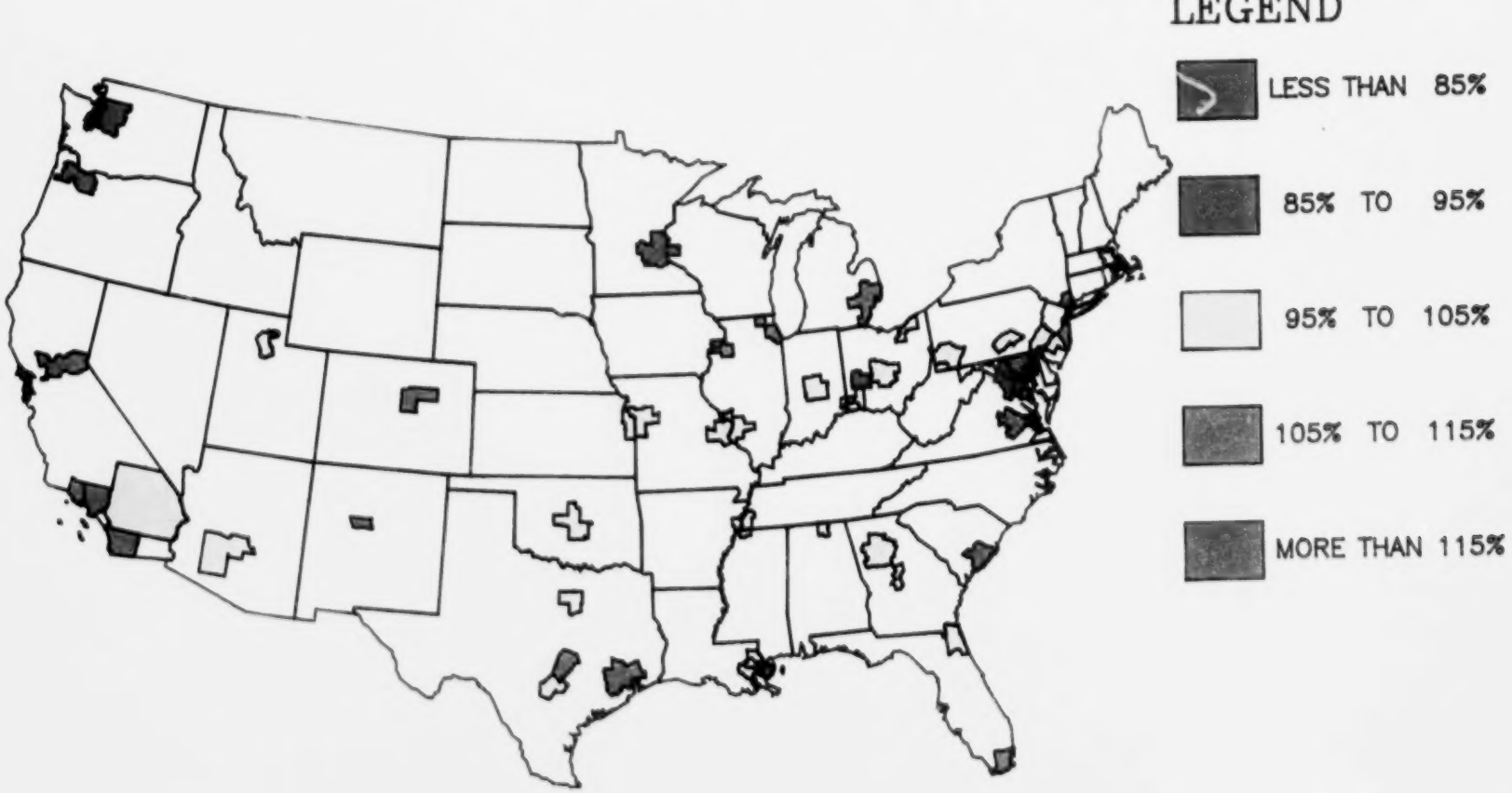

Exhibit III

CLERICAL POSITIONS

PRIVATE SECTOR PAY RELATIVE TO FEDERAL PAY

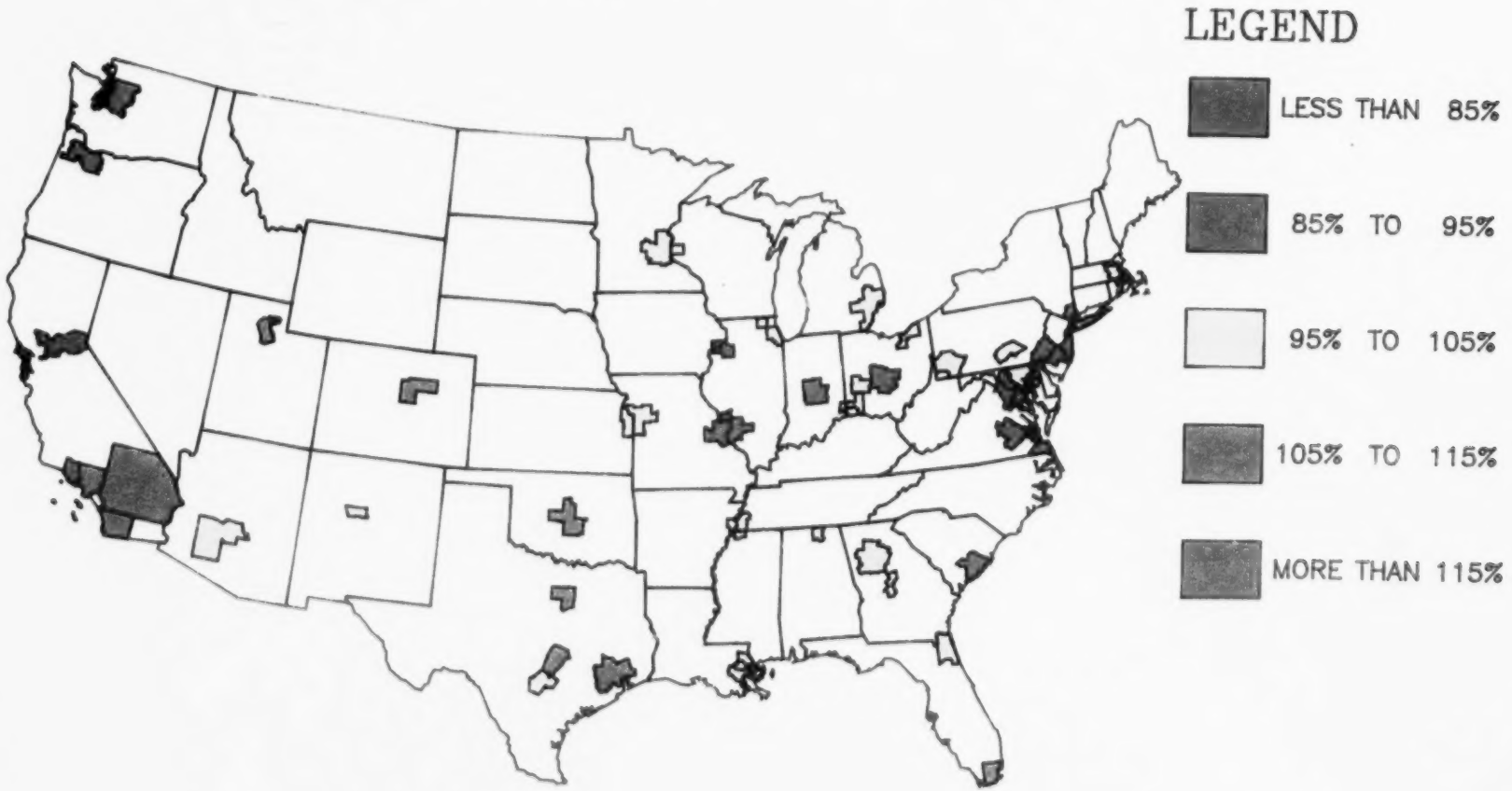

Exhibit IV

TECHNICAL POSITIONS

PRIVATE SECTOR PAY RELATIVE TO FEDERAL PAY

Exhibit V

- Federal vs. Private Sector Salaries for Selected Benchmark Jobs

The general comparison of federal and private sector pay levels is consistent with recent government analyses. Exhibit VI shows the comparison at the national level for a sample of benchmark jobs at each GS grade level. For this purpose the "MSA average" is the simple, unweighted average of the mean salaries reported by MSA. (Survey data are not provided for each benchmark in all MSA's.)

Significantly, private sector salary levels exceed federal levels by at least 20 percent for 30 of the 51 benchmark positions. The pay "gap" is 30 percent or more for 16 of the benchmarks.

Exhibit VI also shows the range of salaries that were used in calculating the national average. The federal mean is lower than the lowest salary in the range for 35 of the 51 benchmark positions.

The range of salaries is illustrative of the variation in pay across the country. Typically, the private sector pay levels in the highest MSA exceed pay levels in the lowest MSA by 20 to 30 percent. For a few, the difference exceeds 50 percent.

Exhibit VII summarizes the distribution of salaries for these benchmark positions.

COMPARATIVE SALARIES
FOR SELECTED BENCHMARK JOBS
FEDERAL VS. PRIVATE SECTOR

Salary Grade	Series	Federal Mean	MSA Average[1]	Percent Difference	Inter-city Private Sector Range
GS-3					
303	Miscellaneous Clerk	$13,578	$16,752	23.4%	$14,771 - $19,406
305	Mail & File	$13,647	$16,901	23.8%	$13,306 - $19,732
322	Clerk Typist	$12,610	$17,884	41.8%	$15,723 - $21,194
356	Data Transcriber	$13,075	$17,588	34.5%	$15,824 - $20,679
GS-4					
203	Personnel Clerk	$14,652	$19,078	30.2%	$17,137 - $26,921
318	Secretary	$14,748	$18,215	23.5%	$16,345 - $20,103
322	Clerk Typist	$14,835	$17,929	20.9%	$14,652 - $22,517
525	Accounting Technician	$14,812	$19,775	33.5%	$17,332 - $22,781
1106	Procurement Clerk	$14,797	$18,268	23.5%	$14,736 - $23,160
GS-5					
203	Personnel Clerk	$16,932	$20,746	22.5%	$17,944 - $23,358
318	Secretary	$17,237	$19,545	13.4%	$17,374 - $22,255
334	Computer Specialist	$16,275	$24,159	48.4%	$22,183 - $26,030
335	Computer Clerk	$17,385	$23,030	32.5%	$18,186 - $26,291
1105	Purchasing	$16,924	$23,864	41.0%	$21,779 - $26,979

[1]MSA average is the simple, unweighted mean of MSA means where actual data are reported.

THE Wyatt COMPANY

Exhibit VI

COMPARATIVE SALARIES
FOR SELECTED BENCHMARK JOBS
FEDERAL VS. PRIVATE SECTOR

Salary Grade	Series	Federal Mean	MSA Average	Percent Difference	Inter-city Private Sector Range
GS-6					
203	Personnel Clerk	$19,218	$21,207	10.3%	$17,983 - $23,302
318	Secretary	$19,644	$22,045	12.2%	$20,512 - $24,157
332	Computer Operator	$18,905	$22,641	19.8%	$20,314 - $26,211
525	Accounting Technician	$19,593	$22,456	14.6%	$15,891 - $27,096
GS-7					
318	Secretary	$22,333	$24,592	10.1%	$20,999 - $27,556
334	Computer Specialist	$20,586	$27,456	33.3%	$26,075 - $30,070
511	Auditing	$21,540	$25,593	18.8%	$21,786 - $28,851
802	Engineering Technician	$23,092	$30,853	33.6%	$26,725 - $34,110
1102	Contracting	$19,722	$29,047	47.3%	$26,071 - $32,597
GS-8					
318	Secretary	$24,869	$29,179	17.3%	$25,506 - $32,236
332	Computer Operator	$24,013	$24,011	0.0%	$20,255 - $29,958
802	Engineering Technician	$23,848	$29,068	21.9%	$25,020 - $32,527

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COMPARATIVE SALARIES
FOR SELECTED BENCHMARK JOBS
FEDERAL VS. PRIVATE SECTOR

Salary Grade	Series	Federal Mean	MSA Average	Percent Difference	Inter-city Private Sector Range
GS-9					
201	Personnel Management	$24,414	$28,981	18.7%	$25,688 - $31,422
334	Computer Specialist	$24,185	$31,728	31.2%	$28,999 - $35,025
511	Auditing	$25,896	$32,408	25.1%	$29,318 - $38,873
610	Nurse	$26,264	$27,480	4.6%	$23,811 - $35,452
1102	Contracting	$24,153	$34,796	44.1%	$29,064 - $39,628
GS-11					
235	Employee Development	$32,386	$33,882	4.6%	$30,589 - $38,156
510	Accounting	$30,423	$37,599	23.6%	$33,986 - $42,655
560	Budget Analysis	$30,839	$32,810	6.4%	$26,793 - $42,222
905	General Attorney	$28,590	$44,593	56.0%	$41,492 - $49,897
1320	Chemistry	$32,628	$41,551	27.3%	$32,214 - $46,732
GS-12					
201	Personnel Management	$38,222	$46,685	22.1%	$35,890 - $51,852
334	Computer Specialist	$37,685	$43,083	14.3%	$38,315 - $47,003
511	Auditing	$37,142	$36,709	-1.2%	$30,442 - $42,680
830	Mechanical Engineering	$38,476	$45,453	18.1%	$40,762 - $50,875
905	General Attorney	$35,612	$53,704	50.8%	$47,122 - $60,131

THE Wyatt COMPANY

COMPARATIVE SALARIES
FOR SELECTED BENCHMARK JOBS
FEDERAL VS. PRIVATE SECTOR

Salary Grade	Series	Federal Mean	MSA Average	Percent Difference	Inter-city Private Sector Range
GS-13					
201	Personnel Management	$46,952	$56,887	21.2%	$47,938 - $73,252
334	Computer Specialist	$45,290	$49,315	8.9%	$41,909 - $53,906
510	Accounting	$46,148	$53,941	16.9%	$41,388 - $70,555
855	Electronics Engineering	$46,727	$55,060	17.8%	$50,145 - $59,945
905	General Attorney	$43,433	$65,720	51.3%	$58,277 - $70,266
GS-14					
201	Personnel Management	$58,291	$70,885	21.6%	$60,818 - $86,120
334	Computer Specialist	$53,640	$56,091	4.6%	$50,602 - $64,303
905	General Attorney	$53,681	$81,625	52.1%	$75,559 - $87,000
GS-15					
511	Auditing	$66,181	$74,599	12.7%	$67,764 - $79,648
905	General Attorney	$64,748	$118,956	83.7%	$105,698 - $147,457

THE Wyatt COMPANY

DISTRIBUTION OF LOCAL AVERAGE SALARIES COMPARED TO MSA AVERAGE

Salary Grade	Series	Less Than 85%	85% to 95%	95% to 105%	105% to 115%	More Than 115%
GS-3						
303	Miscellaneous Clerk	0.0%	33.3%	46.6%	13.3%	6.6%
305	Mail File	7.7%	30.8%	23.1%	23.1%	15.4%
322	Clerk Typist	0.0%	33.3%	46.6%	0.0%	20.0%
356	Data Transcriber	0.0%	28.6%	42.9%	21.4%	7.1%
GS-4						
203	Personnel Clerk	0.0%	46.6%	33.3%	13.3%	6.6%
318	Secretary	0.0%	26.7%	46.6%	26.7%	0.0%
322	Clerk Typist	6.6%	26.7%	26.7%	33.3%	6.6%
522	Accounting Technician	0.0%	35.7%	42.9%	14.3%	7.1%
1106	Procurement Clerk	6.6%	26.7%	40.0%	6.6%	20.0%
GS-5						
203	Personnel Clerk	0.0%	21.4%	50.0%	28.6%	0.0%
318	Secretary	0.0%	20.0%	60.0%	20.0%	0.0%
334	Computer Specialist	0.0%	22.2%	55.6%	22.2%	0.0%
335	Computer Clerk	12.5%	25.0%	12.5%	50.0%	0.0%
1105	Purchasing	0.0%	15.4%	61.5%	23.1%	0.0%

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DISTRIBUTION OF LOCAL AVERAGE SALARIES COMPARED TO MSA AVERAGE

Salary Grade	Series	Less Than 85%	85% to 95%	95% to 105%	105% to 115%	More Than 115%
GS-6						
203	Personnel Clerk	7.7%	23.1%	28.6%	35.7%	0.0%
318	Secretary	0.0%	13.3%	66.7%	20.0%	0.0%
332	Computer Operator	0.0%	30.8%	38.5%	23.1%	7.7%
525	Accounting Technician	12.5%	12.5%	37.5%	25.0%	12.5%
GS-7						
318	Secretary	0.0%	26.7%	53.3%	20.0%	0.0%
334	Computer Specialist	0.0%	6.6%	80.0%	13.3%	0.0%
511	Auditing	0.0%	16.6%	41.7%	41.7%	0.0%
802	Engineering Technician	0.0%	22.2%	11.1%	33.3%	0.0%
1102	Contracting	0.0%	7.1%	71.4%	21.4%	0.0%
GS-8						
318	Secretary	0.0%	14.3%	64.3%	21.4%	0.0%
332	Computer Operator	7.7%	23.1%	53.8%	0.0%	15.4%
802	Engineering Technician	0.0%	50.0%	0.0%	50.0%	0.0%

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DISTRIBUTION OF LOCAL AVERAGE SALARIES COMPARED TO MSA AVERAGE

Salary Grade	Series	Less Than 85%	85% to 95%	95% to 105%	105% to 115%	More Than 115%
GS-9						
201	Personnel Management	0.0%	33.3%	22.2%	44.4%	0.0%
334	Computer Specialist	0.0%	15.4%	69.2%	15.4%	0.0%
511	Auditing	0.0%	28.6%	57.1%	7.1%	7.1%
610	Nurse	0.0%	35.7%	30.8%	23.1%	7.7%
1102	Contracting	7.1%	7.1%	64.3%	21.4%	0.0%
GS-11						
235	Employee Development	0.0%	16.6%	75.0%	8.3%	0.0%
510	Accounting	0.0%	14.3%	64.3%	21.4%	0.0%
560	Budget Analysis	18.2%	18.2%	27.3%	27.3%	9.0%
905	General Attorney	0.0%	25.0%	41.7%	33.3%	0.0%
1320	Chemistry	12.5%	37.5%	25.0%	25.0%	0.0%
GS-12						
201	Personnel Management	7.1%	28.6%	14.3%	50.0%	0.0%
334	Computer Specialist	0.0%	20.0%	66.7%	13.3%	0.0%
511	Auditing	9.0%	9.0%	63.6%	9.0%	9.0%
830	Mechanical Engineering	0.0%	36.3%	36.3%	27.3%	0.0%
905	General Attorney	0.0%	20.0%	53.3%	26.7%	0.0%

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DISTRIBUTION OF LOCAL AVERAGE SALARIES COMPARED TO MSA AVERAGE

Salary Grade	Series	Less Than 85%	85% to 95%	95% to 105%	105% to 115%	More Than 115%
GS-13						
201	Personnel Management	9.0%	27.3%	45.5%	9.0%	9.0%
334	Computer Specialist	6.6%	6.6%	60.0%	26.7%	0.0%
510	Accounting	9.0%	18.2%	36.3%	18.2%	18.2%
855	Electronic Engineering	0.0%	28.6%	42.9%	28.6%	0.0%
905	General Attorney	0.0%	15.4%	61.5%	23.1%	0.0%
GS-14						
201	Personnel Management	0.0%	37.5%	62.5%	0.0%	0.0%
334	Computer Specialist	0.0%	20.0%	60.0%	20.0%	0.0%
905	General Attorney	0.0%	27.3%	45.5%	27.3%	0.0%
GS-15						
511	Auditing	0.0%	14.3%	71.4%	14.3%	0.0%
905	General Attorney	11.1%	22.2%	22.2%	33.3%	11.1%

Note: Percentages based on actual survey data as reported for fourteen cities. Data not reported for each series in all cities.

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- Market Pay Levels by Salary Grade

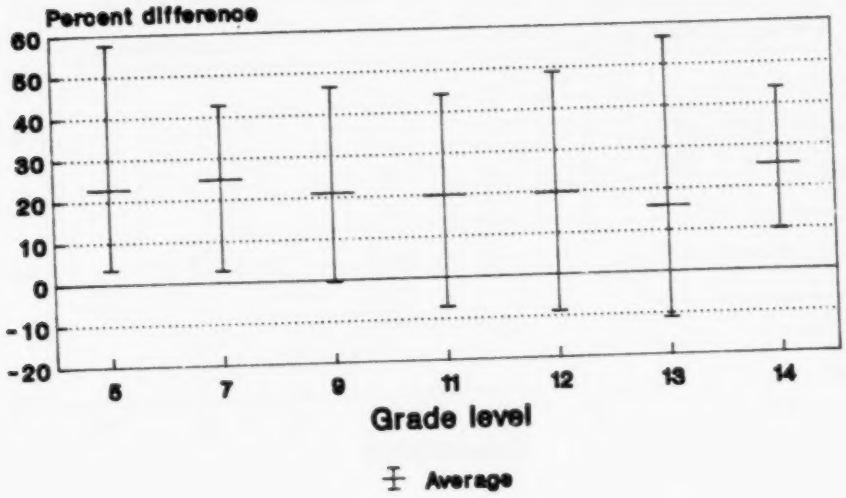
Exhibit VIII illustrates the distribution of market levels from a different perspective. We have selected ten series for which survey data are available in a large number of MSA's. The graphs compare the actual private sector average (for the MSA's where actual data are reported) with the federal mean pay at each GS grade.

Since the graphs are not self-explanatory, it is important to point out that there are three market levels shown for each grade. The middle mark on each bar denotes the MSA average, while the marks at the top and bottom denote the highest and lowest MSA (for which data are reported). On each graph, the federal average is the solid, zero percent difference line.

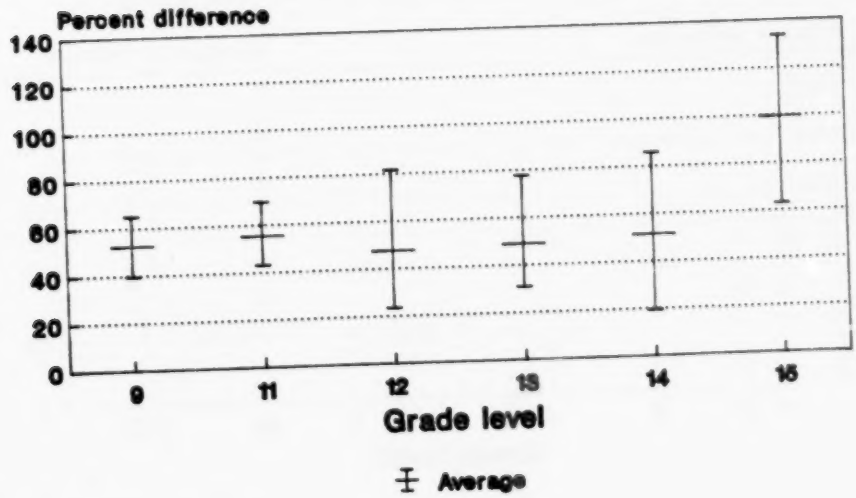
The graphs illustrate that:

- the MSA averages "mask" substantial variation in pay across occupations and grade level;
- each series has a distinctive pattern;
- federal salaries are consistently below private sector salaries (although it is worth noting that there is more overlap than is apparent because of the distribution of actual salaries around both the federal and private sector means);
- the gap for some series is consistently large (e.g., general attorney), while for others it is not significant (e.g., computer operation); and
- the gap is comparable across the salary grades.

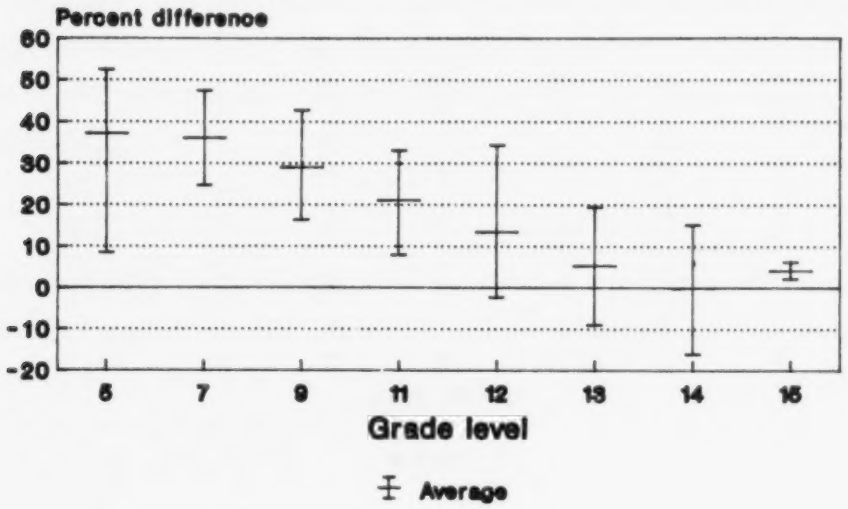
Accountant
Excess of local over federal pay



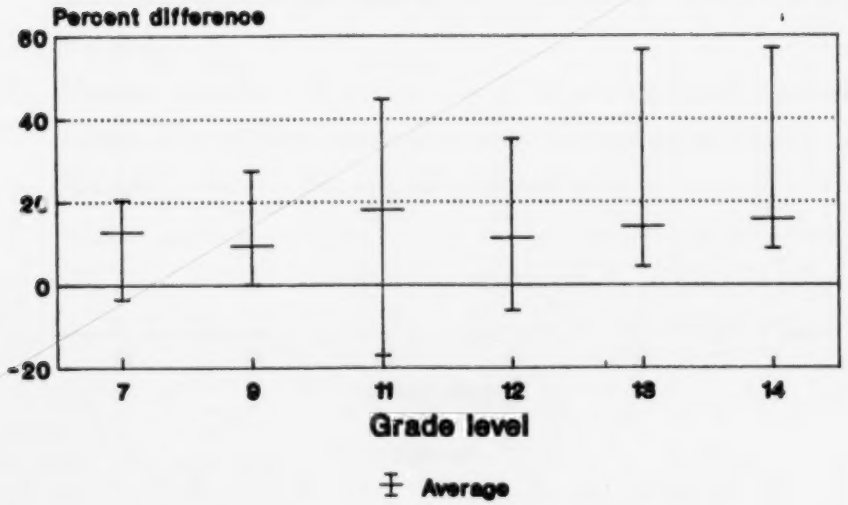
General Attorney
Excess of local over federal pay



Computer Specialist
Excess of local over federal pay

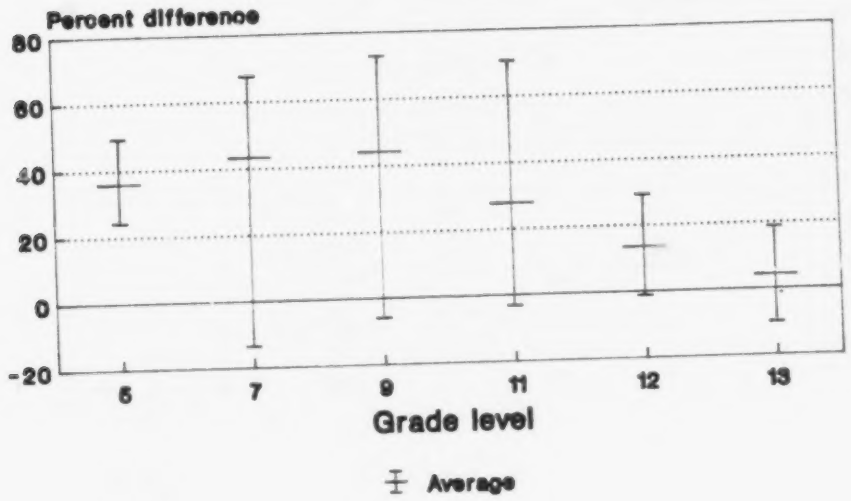


Personnel Management
Excess of local over federal pay



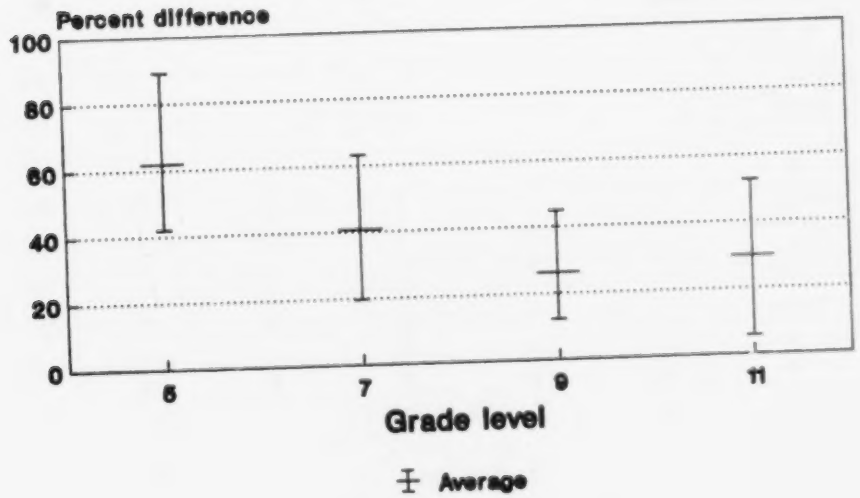
Contracting

Excess of local over federal pay



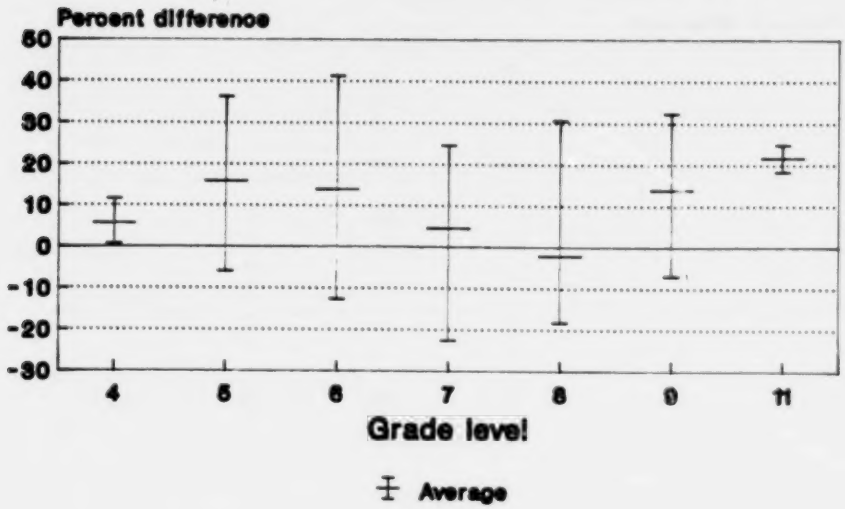
Engineering Technician

Excess of local over federal pay



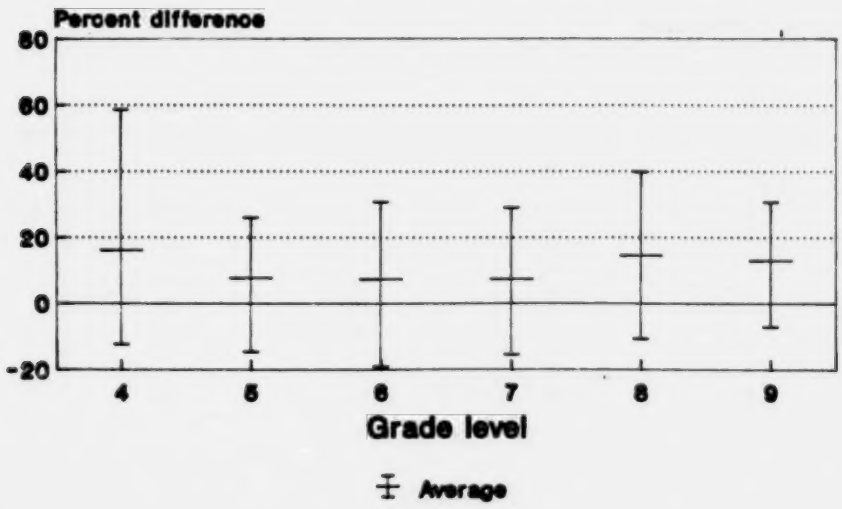
Computer Operation

Excess of local over federal pay

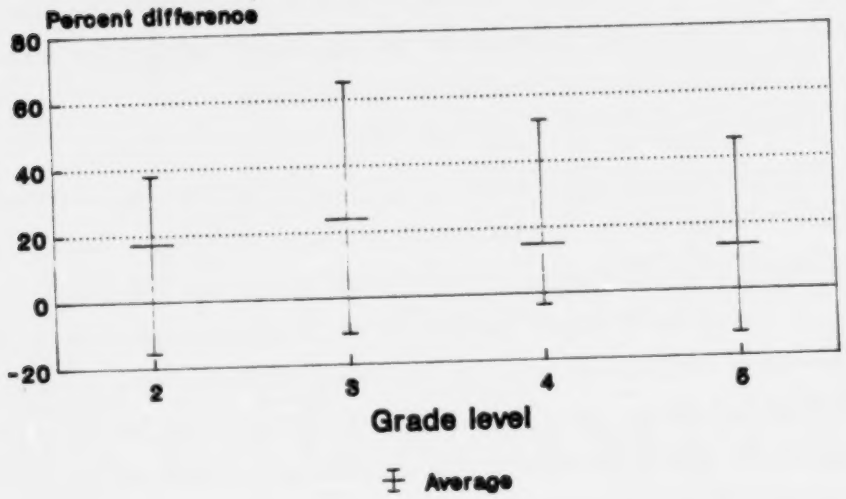


Secretary

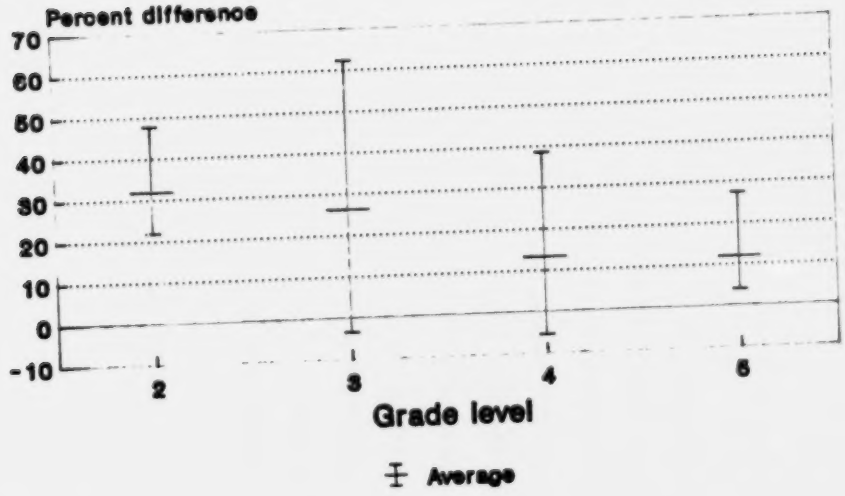
Excess of local over federal pay



Clerk-Typist
Excess of local over federal pay



Data Transcriber
Excess of local over federal pay



- Private Sector Job Hierarchy

The federal salary program is based on the premise that the job hierarchy should be consistent across the country. That is to say, comparable jobs are always assigned to the same salary grades so that individual salaries for a series are in essentially the same relative position on the hierarchy.

The private sector job hierarchy, in contrast, is the composite of the hierarchies established by numerous independent employers. Each reacts to the shifting supply of workers based on their staffing strategy and needs, and adjusts salaries, as necessary, to ensure that they maintain an adequate staff. In each local area, the mix of industries and their recent growth or decline affects the demand for occupational specialties. The dynamics of these labor market forces govern relative salary levels. In light of the often dramatic differences in the local economies across the country, it is not surprising that there are significant differences in both the salary levels and the job hierarchies, from labor market to labor market.

Exhibit IX shows the job hierarchy for selected Professional and Administrative jobs, with the hierarchy expressed as the ratio of each job's mean salary compared with the pay for a base job, across eight cities. Exhibit X shows a similar listing for selected Clerical and Technical jobs. Two jobs were selected at each of five GS-grade levels.

FEDERAL VS PRIVATE SECTOR JOB HIERARCHIES EXPRESSED AS COMPARATIVE SALARY RATIOS PROFESSIONAL AND ADMINISTRATIVE JOBS

Series (Grade)	Federal	Atlanta	Boston	Chicago	Dallas	Los Angeles	New York	Philadelphia	Washington
334 Computer Specialist (7)	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
511 Auditing (7)	1.05	.34	.99	.92	.94	.85	.88	.81	1.01
334 Computer Specialist (9)	1.18	1.28	1.13	1.19	1.14	1.16	1.15	1.12	1.13
510 Accounting (9)	1.31	1.03	1.13	.99	1.09	1.04	1.10	1.06	1.05
201 Personnel Management (13)	1.51	.99	1.13	1.42	1.38	1.33	1.43	1.39	1.52
110 Economist (11)	1.50	1.25	1.49	1.34	1.10	1.39	1.32	1.30	1.59
334 Computer Specialist (12)	1.83	1.58	1.65	1.60	1.58	1.56	1.64	1.50	1.58
905 General Attorney (12)	1.73	1.86	2.06	1.96	1.99	1.89	1.94	1.92	2.04
201 Personnel Management (12)	2.28	1.84	2.10	1.86	2.02	1.78	2.05	2.07	1.94
510 Accounting (13)	2.24	1.59	2.03	1.87	1.99	1.80	2.04	1.84	1.83

Note: Ratios are determined by dividing the mean salary for each job by the mean salary for the comparison jobs: Mail and File Clerk (GS-3) for Clerical and Technical Jobs, and Computer Specialist (GS-7) for Professional and Administrative jobs.

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Exhibit IX

FEDERAL VS PRIVATE SECTOR JOB
HIERARCHIES EXPRESSED AS COMPARATIVE SALARY RATIOS
CLERICAL AND TECHNICAL

Series (Grade)	Federal	Atlanta	Boston	Chicago	Dallas	Los Angeles	New York	Philadelphia	Washington
305 Mail & File (3)	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
356 Data Transcriber (3)	.96	.99	1.26	1.18	.95	.97	1.09	.99	1.04
318 Secretary (4)	1.08	1.14	1.28	1.28	.91	.99	1.18	.99	1.08
525 Accounting Technician (4)	1.09	1.30	1.30	1.27	1.03	1.08	1.18	1.08	1.31
322 Clerk Typist (5)	1.23	1.32	1.41	1.47	1.11	1.18	1.50	1.05	1.15
525 Accounting Technician (5)	1.26	1.57	1.48	1.48	1.26	1.22	1.51	1.18	1.35
318 Secretary (6)	1.44	1.51	1.59	1.49	1.15	1.24	1.42	1.25	1.32
332 Computer Operations (6)	1.39	1.57	1.67	1.56	1.14	--	1.43	1.20	1.24
318 Secretary (7)	1.64	1.59	1.87	1.68	1.33	1.41	1.64	1.35	1.44
203 Personnel Clerical Assistance (7)	1.55	1.69	2.16	1.78	1.54	1.41	1.78	1.43	1.67

Note: Ratios are determined by dividing the mean salary for each job by the mean salary for the comparison jobs: Mail and File Clerk (GS-3) for Clerical and Technical Jobs, and Computer Specialist (GS-7) for Professional and Administrative jobs.

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Exhibit X

For the Professional and Administrative jobs, all salaries are compared with the local market average for 334-Computer Specialist (GS-7). For the Clerical and Technical jobs, the comparison job is 305-Mail & File (GS-3).

As expected, the federal job hierarchy shows the ratios for jobs in the same grade to be roughly equal.

Across the eight cities, however, there are some dramatic differences. It is important to appreciate that the ratios in each city are affected by the relative pay for the comparison job. In Boston, for example, the Mail & File Clerk is lower paid relative to the other jobs, which increases the ratios for several of the jobs.

The private sector job hierarchies show notable differences from the federal pattern. For example, the Auditing (GS-7) and Accounting (GS-9) jobs are paid less across the cities than the Computer Specialists in both grades. Similarly, the private sector generally pays the Personnel Clerical Assistant (GS-7) job more than a Secretary (GS-7), but the government assigns them to the same grade.

The data suggest that the private sector "values" lawyers (the average ratio is 1.96) more than does the government (ratio of 1.73). In contrast, the government values economists (ratio of 1.50) more than does the private sector (the average ratio is 1.35).

Differences of this type may be significant when the government needs to recruit in a metropolitan area. The government's job hierarchy, as established by title 5 U.S.C., is incorporated into the classifications/job evaluation process, which dictates the salary grade for each position. The differences in the job hierarchies suggest that a private sector employer would assign some of the jobs to different salary grades, even if the overall salary programs were equivalent. In some cases, as with the economists, the government would be paying more than the private sector while in others the government's salary range would be below the market pay

levels. The government's continued adherence to a fixed job hierarchy could affect its ability to compete. Unless there is a change in this policy , this problem may be insolvable.

- Starting Salaries for College Graduates

Although it is an issue peripheral to this study, one of the government's basic staffing problems is its annual need to recruit a large number of recent college graduates. The government's practice is to start graduates (with undergraduate degrees) at GS-5, although graduates in selected fields can start at GS-7. The current Step 1 (the starting salary) of GS-5 is $15,738. (GS-7, Step 1 is $19,493.)

These salary levels are significantly below current market levels. In a recent survey, the Northwestern Lindquist-Endicott Report (1989), the average starting salaries for graduates in selected academic fields were reported as follows:

Engineering	$30,612
Accounting	26,568
Sales/Marketing	25,572
Business Administration	24,372
Liberal Arts	24,347
Computer	27,756
Chemistry	28,488
Math/Statistics	26,342
Economics/Finance	25,332
Other Fields	25,272

For the lowest-paid field, liberal arts, the national average is 55 percent above the government's GS-5 starting salary. If the government assigned these graduates to the grade that is closest to the survey average, it would be reasonable to select GS-9, where Step 1 is $23,846.

Using this logic, recent graduates in the other fields could be assigned to GS-10 or 11.

APPENDIX

SALARY SURVEY SOURCES

Bureau of Labor Statistics

Professional Administrative Technical Clerical (PATC) Survey
Unpublished BLS combined PATC/AWS surveys for 29 MSA's

Executive Compensation Service (ECS)

Professional and Scientific Personnel Report
Hospital and Health Care Report
Technical and Skilled Trades Personnel Report
Office Personnel Report

Mercer Meidinger Hansen

Human Resources Survey
Data Processing Survey
Finance and Accounting Survey
Material Logistics Survey

BENCHMARK SERIES IN OPM SURVEY DATABASE

Professional Series

110 Economist
510 Accounting
511 Auditing
512 Internal Revenue Agent
610 Nurse
801 General Engineering
810 Civil Engineering
830 Mechanical Engineering
850 Electrical Engineering
855 Electronics Engineering
893 Chemical Engineering
896 Industrial Engineering
905 General Attorney
1320 Chemistry
1410 Librarian

Administrative Series

18 Safety & Occupational Health Management
80 Security Administration
201 Personnel Management
212 Personnel Staffing
221 Position Classification
223 Salary & Wage Administration
230 Employee Relations
233 Labor Relations
235 Employee Development
260 Equal Employment Opportunity
301 Miscellaneous Administration & Programs
334 Computer Specialist
342 Support Services Administration
343 Management Analyst
345 Program Analyst
391 Communications Management
501 Financial Data Systems Specialist
505 Financial Management
560 Budget Analysis
950 Paralegal Specialist
1035 Public Affairs
1082 Writing & Editing
1083 Technical Writing & Editing
1102 Contracting
1150 Industrial Specialist
1160 Financial Analysis
1165 Loan Specialist
1910 Quality Assurance
2010 Inventory Management
2130 Traffic Management

Technical Series

203 Personnel Clerical Assistance
303 Miscellaneous Clerk and Assistant
332 Computer Operation
335 Computer Clerk and Assistance
392 General Communications
393 Communications Specialist
503 Financial Clerk and Assistance
525 Accounting Technician
620 Practical/Vocational Nurse
621 Nursing Assistant
802 Engineering Technician
818 Engineering Drafting
856 Electronics Technician
1060 Photography
1105 Purchasing
1106 Procurement Clerk and Assistance
1152 Production Control
1311 Physical Science Technician
2005 Supply Clerical and Technician

Clerical Series

203 Personnel Clerical Assistance
303 Miscellaneous Clerk and Assistant
305 Mail and File
312 Clerk-Stenographer and Reporter
318 Secretary
322 Clerk-Typist
335 Computer Clerk and Assistance
350 Equipment Operator
356 Data Transcriber
382 Telephone Operating
503 Financial Clerk and Assistance
525 Accounting Technician
544 Payroll
998 Claims Clerical
1106 Procurement Clerk and Assistance
1802 Compliance Inspection and Support
2005 Supply Clerical and Technician
2132 Travel

BENCHMARK SERIES IN OPM SURVEY DATABASE

Professional Series

110 Economist
510 Accounting
511 Auditing
512 Internal Revenue Agent
610 Nurse
801 General Engineering
810 Civil Engineering
830 Mechanical Engineering
850 Electrical Engineering
855 Electronics Engineering
893 Chemical Engineering
896 Industrial Engineering
905 General Attorney
1320 Chemistry
1410 Librarian

Administrative Series

18 Safety & Occupational Health Management
80 Security Administration
201 Personnel Management
212 Personnel Staffing
221 Position Classification
223 Salary & Wage Administration
230 Employee Relations
233 Labor Relations
235 Employee Development
260 Equal Employment Opportunity
301 Miscellaneous Administration & Programs
334 Computer Specialist
342 Support Services Administration
343 Management Analyst
345 Program Analyst
391 Communications Management
501 Financial Data Systems Specialist
505 Financial Management
560 Budget Analysis
950 Paralegal Specialist
1035 Public Affairs
1082 Writing & Editing
1083 Technical Writing & Editing
1102 Contracting
1150 Industrial Specialist
1160 Financial Analysis
1165 Loan Specialist
1910 Quality Assurance
2010 Inventory Management
2130 Traffic Management

Technical Series

203 Personnel Clerical Assistance
303 Miscellaneous Clerk and Assistant
332 Computer Operation
335 Computer Clerk and Assistance
392 General Communications
393 Communications Specialist
503 Financial Clerk and Assistance
525 Accounting Technician
620 Practical/Vocational Nurse
621 Nursing Assistant
802 Engineering Technician
818 Engineering Drafting
856 Electronics Technician
1060 Photography
1105 Purchasing
1106 Procurement Clerk and Assistance
1152 Production Control
1311 Physical Science Technician
2005 Supply Clerical and Technician

Clerical Series

203 Personnel Clerical Assistance
303 Miscellaneous Clerk and Assistant
305 Mail and File
312 Clerk-Stenographer and Reporter
318 Secretary
322 Clerk-Typist
335 Computer Clerk and Assistance
350 Equipment Operator
356 Data Transcriber
382 Telephone Operating
503 Financial Clerk and Assistance
525 Accounting Technician
544 Payroll
998 Claims Clerical
1106 Procurement Clerk and Assistance
1802 Compliance Inspection and Support
2005 Supply Clerical and Technician
2132 Travel

STUDY OF FEDERAL EMPLOYEE LOCALITY PAY

TASK 4: *Interpreting The Relevance Of Non-Federal Practices And Identifying Alternative Federal Pay Systems*

TASK 4 - INTERPRETING THE RELEVANCE OF NON-FEDERAL PRACTICES AND IDENTIFYING ALTERNATIVE FEDERAL PAY SYSTEMS

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APPROACH TO THIS TASK

The initial step in this Task was to assemble a five-member Technical Advisory Committee for a two-day meeting in Washington. The members of the Committee are among the most prominent academic researchers and consultants in the field of compensation management in the country. They are active in the American Compensation Association, serving as seminar leaders and frequent speakers. Four of the five are authors or co-authors of textbooks, and all five have contributed numerous articles to professional journals. The members of the Committee are:

- Dr. George Milkovich, Cornell University
- Dr. Richard Henderson, Georgia State University
- Dr. Charles Fay, Rutgers University
- Dr. James Beatty, San Diego State University
- Dr. Marc Wallace, University of Kentucky

Prior to the meeting, previously generated analyses of the OPM database along with background materials on the GS salary program were forwarded to the Committee members.

Our objective as a group was to discuss alternative program concepts and the methodologies for maintaining a revised program. During the time since the meetings were held, the Committee members have continued to react to new or revised concepts, and to suggest refinements to the basic program concepts.

We have, in turn, discussed the basic concepts in meetings with government representatives.

OVERVIEW OF RECOMMENDATIONS

We recommend that the government consider the following changes in its white-collar salary program:

- Create "local" salary programs for Clerical, Technical and Other series employees.

Employees in these positions are often recruited from areas within a few miles of their work locations. The actual distance is dependent on commutation alternatives, and the time required to commute from home to work location. The relevant labor market can be defined with geographic boundaries that reflect the limits of the commuting patterns. In most areas of the country, it would be unusual for employees in these positions to commute more than 15 to 20 miles. These limits define the "local labor markets."

As our surveys of corporate practice show, maintaining local salary programs for employees in these occupations is virtually a universal practice. In fact, it is rare for corporations to include these occupations under the same salary program with professional and administrative occupations. This practice is related to the labor market differences as well as the legal distinctions between "exempt" and "non-exempt" workers. The few corporations in our surveys that use national salary schedules recognize that they are paying higher salaries in some areas than is necessary.

- Professional and administrative employees should continue to be paid within a national salary schedule, but provide for geographic differentials for employees in high-pay areas. Based on the analysis of the survey database, we recommend initially considering New York and its environs, Los Angeles, San Francisco, and possibly Boston and Washington, D.C. as high-pay areas.

Survey data show that there are variations in the prevailing pay levels for professional and administrative occupations across the country, although the differences among most regions are not significant. The relevant labor markets for these positions are larger than for clerical and technical positions but, realistically, it is invalid to assume that the markets can be defined as multi-state regions.

Prevailing salary levels in the three areas cited are significantly above the national "norm," and it will be advantageous to reflect this in pay levels. We recommend that any increase in pay be treated as a differential paid in addition to salary.

It will be important to confirm our conclusions with more extensive surveys. Over time, other metropolitan areas may indicate that salary differentials are necessary, and the legislation should provide flexibility to respond to these situations.

It may be necessary to continue differentials for Hawaii and Alaska, but adequate survey data is not readily available to allow us to confirm this.

- Both the national schedule for professional and administrative series and the local schedules for clerical, technical and other series should be established so pay levels are comparable to prevailing median pay levels in the relevant labor markets.

This represents a reconfirmation of the government's compensation philosophy. In fact, paying clerical and technical employees on a local basis is a more valid interpretation of this philosophy. There needs to be a renewed commitment to this policy.

No employee should experience a salary cut because of the introduction of locality pay. Employees paid above prevailing rates should receive smaller increases during the phase-in period until their pay rates are in line with their local community.

- The basis for establishing the local salary schedules should be area surveys conducted by the Bureau of Labor Statistics.

The BLS already conducts area surveys in roughly 90 metropolitan areas. We recommend that the list of "benchmark" jobs be expanded to be more representative of the technical positions, but in other respects their methodology is sound and should be continued. We further recommend that area surveys be conducted every three years, rather than every year. In order to distribute the workload, this could be evenly divided over the three years. The annual salary schedule adjustment for the years between surveys should be based on the BLS Employment Cost Index (ECI) which measures increases in "labor costs."

While the approach we are recommending is basically consistent with the Federal Wage System methodology, we believe it will be important to have the surveys conducted by the BLS. The BLS surveys are unquestionably the best in the country, and they are perceived as valid throughout government. By building on existing surveys, it should minimize the costs and ensure corporate participation. In our opinion, private sector employers might not be willing to participate in a new round of government surveys.

- The national schedule for professional and administrative positions should also be based on a BLS survey.

This should be an expanded and revised version of the Professional, Administrative, Technical and Clerical (PATC) Survey. There will, of course, no longer be a need to report data for clerical and technical jobs at the national level. We recommend the list of benchmark professional and administrative positions be expanded to include ones that are representative of government. We believe it will also be important to survey state and local governments. This would be a decidedly different survey.

Realistically, it will require at least two years to develop and test the new survey methodology. Until the BLS and OPM are ready to introduce the new methodology, we recommend using the white-collar component of the ECI to determine the comparability adjustment during this interim period. (Any "catch-up" increases would be in addition to the ECI adjustment.)

- The format of the salary schedules should be basically the same as the current General Schedule, except that the range "spread"--minimum to maximum--should be expanded from 30% to 40%. However, the number of grades for each schedule can be expected to be different because of the differences in the mix of occupations.

The average corporate salary range is wider, but this makes sense only if there is a commitment to a meaningful merit pay program.

The "midpoint" of each range is the link to the labor market. If the structures are properly designed and adjusted annually, employees who progress to midpoint should be paid consistent with the market.

- The salary program should continue to be based on a step progression system to the range midpoint, or wherever in the pay range the policy line is established but pay increases above this level should be dependent on individual performance.

Increasingly across both the private and public sectors, there is a move away from automatic pay adjustments to pay-for-performance systems. Virtually every corporation relies on merit pay for non-bargaining unit employees. The government's experience with these concepts is viewed by many as a failure. In our opinion this track record plus the government's need to draw closer to the appropriate markets makes it difficult if not impossible, at this time, to rely completely on merit pay concepts for salary adjustments.

Under our recommendation, employees whose performance is satisfactory will progress to the midpoint (approximately step 7 of the expanded range) in nine years. This is a continuation of current policy. We further recommend continuation of the Quality Step Increase (QSI) concept to enable the better performers to progress at a faster rate to their salary range midpoints. This means that all fully satisfactory employees will be paid appropriately relative to prevailing salary levels.

Only those employees whose performance is rated as outstanding will be able to progress above midpoint, or above competitive market levels. Based on Wyatt surveys of corporate practice, no more than 15 to 20 percent of the work force should be rated at this level. We believe this approach is fair to both federal employees and the taxpayers.

The managers in GS grades 13, 14 and 15, who are already paid on a merit pay basis, should continue to be eligible for merit increases. We are aware, however, that this system needs some refining.

- Within a salary range, agencies should be authorized to start new hires at step 1, 2 or 3, depending on individual qualifications.

This is an extension of current policy and the flexibility should help agencies in recruiting qualified personnel. Obviously, not all applicants are equal; individuals with better qualifications can command higher salaries. This is true in all occupations.

Step 3 is essentially the first quartile--it is 25 percent of the way through the range--so the discretion is limited. Until the salary ranges are increased to market levels, it may make sense to authorize starting salaries anywhere within the range. As market rates are approached, OPM can regulate to bring practice in line with the above recommendation.

- The government should establish separate salary programs for law enforcement and health care specialists. This may also be appropriate for other occupational groups of non-"white-collar" workers.

As with the salary programs maintained by the intelligence agencies, specialists in health care and law enforcement (or using, in the latter case, a broader definition--the protective occupations) do not fit the concept of white-collar employees who have counterparts in a broad spectrum of other employers across the country. The labor markets for these employees are essentially limited to other public sector employers in the case of law enforcement or to specialized health care institutions. Moreover, the dynamics of the economic forces that govern pay in these labor markets are not the same as those that drive "office" salaries. For example, current salary increase rates for several specialized health care occupations are roughly double the rates for office workers.

This recommendation is also based on the premise that it will be relatively straightforward to develop and maintain separate local salary programs for these series. Hospitals, for example, routinely participate in local surveys, and it should be easy for government health care facilities to become participants. Similarly, it should be possible to establish a hierarchy of jobs in the law enforcement series by using a job evaluation methodology and then pay these workers in relation to state and local pay rates. Within these broad occupational groups, there should be a consistent compensation philosophy across government.

- The broad banding concept should be adopted for administering salaries for "bench" researchers.

While it would be a mistake at this point to delimit the research occupations, we do not want to make it so broad as to encompass every employee who has or could have the word "research" in his/her job title. Our intent is to apply this recommendation to those employees who are working to develop or apply theoretical

knowledge to solve problems or to expand our knowledge. Those employees are being paid for their knowledge and for creative thinking. Employees in research career paths may never change positions; they simply become more proficient and productive in the same problem area. The classification concept, grade level distinctions, and step progression approach are artificial and probably counter-productive for these career paths. (Our view of these positions is basically consistent with the "Research Grade-Evaluation Guide" issued in 1976.)

The broad band concept is based on five logical levels in a researcher's career path. The levels as defined recently for the NIST demonstration project are as follows:

I: Trainee Stage (student trainees)

II: Developmental Stage (undergraduate degree with limited experience)

III: Independent Research Stage (full member status on a research team or entry-level Ph.D. graduates)

IV: Senior Researcher Stage (program and professional leadership responsibility)

V: Authoritative Stage (peer recognition as an authority which extends beyond immediate organization)

These are relevant to virtually all careers in research. We presume that it would be relatively easy to gain peer agreement on an individual's qualifications for promotion from one stage to another. This could be comparable to the college tenure process.

While the broad band concept promises to be effective for researchers, we feel strongly that it is inappropriate for other types of positions. A well-designed and maintained salary structure represents a management control mechanism that provides a framework for managing employee compensation. The typical salary range, with a "spread" of 40 to 50 percent, provides considerable flexibility to manage individual salaries as employees becomes increasingly proficient in their jobs. The

grades represent a meaningful but simple basis for giving recognition to the job hierarchy, or relative job importance, and for rewarding employees as they are promoted up their career ladder. The broad band concept is also highly dependent on merit pay to govern salary increases, but this could quickly become an extended step or automatic increase system in too many agencies. If the federal government converted its pay program to the broad band concept, it would lose its ability to control salaries, and to maintain the standard of internal equity that has been historically important.

- Each agency should be authorized to pay more than the classification system and the GS salary levels would normally permit for a limited number of positions. We recommend that agencies be granted this flexibility for up to 5 percent of their jobs, or 10 percent of their staff, and be authorized to pay these employees up to 15 percent above the GS specified rate.

Critics of the GS program frequently cite its rigidity, and the interest at the agency level in having some degree of flexibility in administering the program. Our recommendation is intended to respond to this need but with reasonable limitations. From our perspective an agency's mission dictates its staffing strategy which in turn dictates its compensation strategy. In practical application, this can be interpreted as the need for higher (or lower) calibre employees in some work units than in others. In keeping with the expectation that higher salaries will, over time, make it possible to recruit better qualified workers, agencies should be able to take advantage of the policy to upgrade the incumbents in key positions that are important to their mission. This recommendation is consistent with the special rates concept.

This recommended change is not intended to obviate the need for the established special rate process. Under our concept, there is no need to justify the increased salaries or to seek OPM approval. While the locality pay concept and the geographic salary differentials should minimize the need for special rates, situations

may arise that necessitate higher salaries for more individuals than allowable under our recommendation.

- The government has an important need to employ "world class" experts in an extremely limited number of senior positions.

We anticipate that there will be no more than 500 positions of this type across government, but the individuals selected to fill this role should be among the "best and brightest" in their fields in the world. The agencies should, from our perspective, be able to pay whatever is necessary to recruit these individuals.

In most cases, the individuals are in academic positions, and their salaries are not substantially above senior executive levels. However, some of the medical researchers command salaries as high as $200,000.

Should the government pay these salaries? If it does not, it may be asked to make a grant to support the same individual doing the same research at his/her home institution. Where this is the case, the grant will typically also pay for institutional overhead, support staff, possibly expensive equipment and supplies, and even new research facilities. The inability to pay competitive salaries can result in greater government expense for less than full-time commitment from a researcher who has other responsibilities to his/her institution.

Virtually all of these individuals will be in mid-career, possibly with strong ties to their home institutions. It may, therefore, be mutually advantageous to limit the period of employment to two to five years, with the understanding that the individual will return to his/her prior employer at the end of the period. Alternatively, the employment period could be extended under new authorization.

A number of agencies have a limited number of positions requiring world-class experts--NIH, NIST, NSF and NASA are obvious examples. From our

perspective, if the government plans to conduct, for example, AIDS research, then it should be able to employ the researchers who can be expected to make the breakthroughs. Artificial salary ceilings should not be allowed to stand in the way.

There will be a need for a review committee to approve these situations.

- The agencies should have funds designated for lump-sum cash awards to reward outstanding performers.

While we understand that under current legislation it is possible to pay performance-based awards to General Schedule employees, if a separate fund is established and used only for performance awards, it will make it possible to make meaningful awards (up to 10 to 15 percent of salary), and to allocate the money to a few truly outstanding employees. We believe cash awards can reinforce and supplement the merit pay concept, and serve to recognize truly meritorious performance. Our recommendation is essentially an extension of the concept used by the government, for almost a decade, with its managers.

From our perspective, merit pay has a negative connotation in the public sector in part due to the underfunding in the early years. In addition, the intent, when it was introduced, may have been to keep money away from the poor performers. This perception was partially corrected in 1984 with the passage of the Performance Management and Recognition System which established a maximum lump sum award fund, for grade 13 to 15 managers and supervisors, at 1.5% of payroll. The intent of these programs in the private sector is to award additional money to the superstars. Employees expect to benefit and want to demonstrate by their performance that they deserve the money. The program can have real incentive value.

We recommend an increase in the lump sum award program for those already covered by merit pay, from 1.5 to 2%, and the establishment of such a program for

all other employees should help to overcome the problem for the government. A prorata share allocated as a separate fund for work groups across each agency may also be appropriate.

Our recommendation to create a separate incentive fund is based on the conviction that monetary incentives can become a positive component of the government's compensation program. With an increase to the existing separate fund, and with the establishment of such a program for all white-collar positions, supervisors can recognize and reward the few outstanding performers without adversely affecting other subordinates. Moreover, the entire program is focused on positive employee behavior. There is a definite need to establish a "quality control" mechanism to minimize supervisor bias and favoritism.

It is essential that employees believe their good performance will be recognized and adequately rewarded. The normal argument used in designing corporate incentive plans is that the potential awards have to be large enough to make a difference in the employee's lifestyle. From this perspective we recommend that awards be no less than 5 percent of salary and as much as 15 percent. (These percentages are below the levels typical in corporate programs.)

- The government should improve its relocation reimbursement policy to provide financial assistance for employees who need to purchase a new residence in a high housing cost area.

The majority of corporations provide some form of mortgage assistance, and with today's real estate markets, it is difficult to justify asking an employee to disrupt his/her life and incur the costs of home ownership in high cost areas. We recommend that the government modify its policies to assist with the necessary down payment and provide a monthly mortgage differential for three years.

While the level of assistance would be related to the comparative values of the employee's current residence and the "average" for a comparable residence in the new area, the aggregate payments should be no more than the amounts payable under the FBI's new policy for New York.

It is particularly important to keep the relocation payments separate from possible geographic salary differentials. Both are definitely necessary in a few locations but dependent on different factors, and calculated using different methodologies.

- Finally, the government has an ongoing need for a high level, "personnel committee of the board," that would meet perhaps twice a year to consider current issues and problems of the compensation program.

Funding the pay program will always be a political problem, and we appreciate that nothing can change this. However, it is apparent that the institutional forums for public review of these problems are not effective. This includes both the Quadrennial Commission and the Advisory Committee on Federal Pay.

There are a number of agencies and committees involved in decisions related to the pay program along with other organizations (such as the unions) who play a role in the process. However, at this stage there is such a high level of distrust that it is fair to state that the working relationships have broken down. Unfortunately no one is in a position to assume the leadership role that will be necessary to gain agreement on the necessary program changes.

It is fundamentally important that the institutional relationship, be rebuilt. The "personnel committee" of the board, however structured, would be expected to provide the leadership, and to serve as a focal point for the confirmation of the problems and for the assessment of alternative solutions. From our perspective, the

committee needs independence, continuity, and access to adequate staff support (or funding to commission studies). Both the Congress and the President should be able to look to this committee for guidance and non-partisan support. In many respects the committee would be expected to function in the capacity of the Civil Service Commission.

Our discussions suggest strongly that it will be essential for someone who is acceptable to and can gain the respect of the primary role players to take the lead in reforming the salary program.

SPECIFIC PROGRAM ISSUES

- Market-Sensitive vs Market-Based Pay Programs

Although these phrases are often used in compensation management, they do not have a precise meaning. At the extreme, with a market-based salary program, each job is assigned to the salary range that approximates the prevailing pay range for the job. Jobs for which adequate survey data is unavailable are judgmentally assigned to ranges using a "whole job" ranking process. The only consideration is the market and the importance of being competitive.

The market-based concept has little, if any, concern with internal equity. If there is a job evaluation system, it may have been designed around the market-derived ranges for benchmark jobs, and used primarily to assign non-benchmark jobs to appropriate ranges. When survey data shows that a job has moved up or down in the job hierarchy, it is assigned to a new range. Numerous employers follow this approach.

This concept is relatively easy to explain to employees. Moreover, its logic is hard to refute in organizations where the need to be competitive is a pervasive element of the culture. Employees who may be dissatisfied with the philosophy have only one recourse--to find a job with an employer which has a more acceptable compensation strategy.

The concept can be defended with a "business-need" argument, although none of the relevant court decisions has examined the methodologies used to determine market rates. The market-based philosophy places heavy emphasis on labor markets, which should necessitate an analysis and specification in geographic or industry terms of relevant markets. For most employers, the markets realistically differ across occupational groups. Few employers, however, are this precise in the use of survey data.

Where an organization uses two or more salary structures for business operations in different industries or geographic locations, it is possible that a market-based approach would result in different salary grades for the same job in each structure. From this perspective, an internal job hierarchy is not formally recognized --grade assignments are dependent on the survey data. If the relative pay for a job is higher in one location than another, it means that it is assigned to a higher grade. The internal ranking is not considered.

The market-sensitive concept, in contrast, attempts to balance the need to be competitive with internal equity. Internal equity is, of course, an abstract concept that cannot be empirically determined. Each employee has a somewhat different view of equity, which may often be self-serving.

For the government, the only broadly acceptable measure of internal equity is the job hierarchy established in 1923, and confirmed explicitly and implicitly in various studies over the years. We recommend that the government continue to "live with" this hierarchy at least until the program is modified to reflect the locality pay concept.

It would be possible to move toward a more highly refined market-based pay program by establishing separate salary structures for selected occupational groups (beyond those already recommended). The series where market demand has dictated above average salary increase rates are widely recognized. Engineers and lawyers are the best examples. However, the history of the GS program and the need to develop a political consensus to change the program dictates against this strategy.

If the government is able to adapt the program to the locality pay concept, it will provide a more realistic picture of the problems that are directly attributable to the existing job hierarchy. When federal salaries are more closely aligned with

market rates, the government will have a better basis for determining if the hierarchy needs to be modified.

- Definition of "Local" Labor Markets

The OPM provided a survey database for 48 of the larger metropolitan areas. Adequate survey data for non-urban areas is currently unavailable. Therefore, our recommendations regarding the definition of the local labor markets are tentative, and will require further study.

The limited survey data indicate that geographic pay differentials for clerical and technical jobs are essentially an urban/non-urban phenomena, with employers in non-urban areas paying less than those in the urban areas. There are, however, areas of economic concentration between cities where the prevailing pay levels are as high as those in the cities. The northeast corridor has a number of non-urban areas that are consistent with this pattern. While federal employees are concentrated in the larger metropolitan areas, the strategy used to establish schedules for employees outside of the urban areas will have to be reasonable and cost-effective.

The recommended conceptual framework for the clerical/technical salary program is similar to the Federal Wage System (FWS). The two programs would be similar in that we recommend separate salary schedules for each "local area," with local surveys conducted periodically to determine the necessary adjustment needed to remain competitive within the local areas. As with the FWS approach, there will need to be a local, interagency contact point to deal with local issues. Each salary schedule would be free to "float" with the local market and, therefore, would not be limited directly to any other schedule.

The primary difference would be that the Bureau of Labor Statistics will be responsible for all data collection and analysis. While the federal unions may be

accorded a role in advising on methodological problems, we do not believe it is feasible to let them have a role in the data collection or in any aspect of the analysis that would enable them to see individual company data. Corporations simply will not agree to participate if the unions have access to their pay information. Our discussions with the unions suggest that they understand this problem.

The FWS pay program currently provides for 135 survey areas, with an "area of application" concept used to cover all U.S. counties under one of the local schedules. The majority of counties have small numbers of federal employees, which makes it impractical and, with assumptions regarding prevailing pay rates in non-survey areas, unnecessary to survey employers in every county.

Although the area of application concept is a practical and realistic solution that should be used with the clerical/technical program, the areas should be defined with adequate knowledge of labor markets and prevailing pay levels. In our judgment, the program can be developed around something significantly less than 135 areas. The final areas will undoubtedly coincide in some states with existing FWS areas but it would be premature to assume that these areas are also relevant to the white-collar work force.

For example, we are very familiar with the labor markets in Pennsylvania, where the BLS currently conducts four Area Wage Surveys (AWS) covering Philadelphia, Pittsburgh, York, and Scranton/Wilkes-Barre. The Philadelphia AWS covers five counties, with a total of 15,565 federal workers in clerical, technical or other positions. The comparable FWS area includes two additional counties, which have Allentown and Bethlehem as the largest towns. The government employs only 123 clerical or technical workers in these counties, so it would be reasonable to include these counties in the Philadelphia AWS. The Pittsburgh AWS covers four counties with 5800 federal clerical/technical employees. The Pittsburgh FWS includes an additional 27 counties (essentially the western third of the state) which would add only 3,040 workers in these series. Two counties, Butler and Erie,

account for 572 and 270 workers respectively. We believe it would be reasonable to follow the FWS geographic boundaries. At the same time, our consulting experience suggests that the remaining central and northeastern sections of the state represent an essentially homogeneous labor market. We would recommend broadening the York AWS to include the Harrisburg area (which would bring in a large number of state employees) but then using the composite of this survey with the Scranton/Wilkes Barre survey as the basis for administering clerical/technical salaries for these broad areas.

While each state will undoubtedly have a few situations that will require somewhat arbitrary decisions, it should be possible from a technical perspective to define local labor market areas across the country. To reiterate, it would be important to develop these areas around the existing AWS regions to minimize the cost of expanding the survey methodology.

To monitor the program and provide for a central "clearing house" for information, we recommend that a committee be created that is roughly comparable to the Prevailing Rate Advisory Committee (PRAC). While there always be minor problems that will need to be resolved, the PRAC concept appears to work well.

- Refinement of the BLS Survey Methodology

The BLS staff takes pride in its professionalism and objectivity, and in the quality of its surveys. We concur and recommend that the new program be built around this capability. Private sector employers would rarely, if ever, commit as much time and money to pay surveys, but then none have the payroll management considerations relevant to the government. Moreover, the government surveys are intended to benefit other employers in all sectors of the economy.

Pay surveys are intended to answer a simple question, "What do we have to pay to hire adequately qualified workers for this position?" They need to be

structured so that survey data is collected from the employers "competing" in the relevant labor markets. From this perspective, it is essential that the survey sample include the full range of employers represented in the labor market. For the same reason, it is important to exclude employers who are not competing for the same personnel.

This consideration makes it essential to expand the survey "population" (from which the survey sample is selected) to include state and local governments. This should provide a more representative sample of the labor markets. This change should make it possible to increase the list of potential benchmark jobs.

It would also make sense to revise the employment size criterion back to the previously used minimum 200 workers for inclusion in the survey population. While there are many areas where the government is competing with small, "mom and pop" employers, federal job requirements and expectations make any job comparisons suspect. Moreover, for the few job "matches" that were found by BLS in the small employers, there was little evidence that it affected the survey results. Consequently, the cost of including these small companies is completely unwarranted.

- Selection of Benchmark Positions

A related consideration is the choice of "benchmark" jobs to be used in the pay surveys. The benchmarks used currently are generic in the sense that they are defined for survey purposes to be generally comparable to many positions in the private sector, without regard to functional specialization. (For example, many attorneys specialize in a narrow legal field, but for survey purposes they are grouped together as attorneys.) The logic used in selecting benchmark jobs has been that (1) the job families have to account for large numbers of federal workers and (2) they have to be found in large numbers in the federal and private sector labor force.

The current benchmarks are listed in Exhibit I.

The expansion of the survey population should make it possible to "match" a significant number of jobs that are unique to the public sector. At this point, there are no data to even estimate how the addition of these jobs will affect the comparative results. At a minimum, it will make it possible to establish a list of benchmarks that are more representative of the federal work force.

It would also be possible to add benchmarks in fields that are normally found only in specialized types of employers. For example, librarians are normally employed by academic institutions, and the public sector. There are, to be sure, corporate librarians but the numbers are small. Similarly, economists are found on college and university faculties, in large financial service firms and on a limited number of corporate planning staffs.

The relevance of faculty positions raises an interesting question. While teaching at an academic institution is clearly not comparable in job content (i.e., the duties and responsibilities are different) to working on a federal staff, for many federal workers in professional series, colleges and universities represent the primary career alternative. It is fully possible to develop a survey methodology that bases comparisons on individual credentials rather than job content. This would be a logical basis for deciding if, for example, meteorologists are paid competitively.

There is a long list of series where workers have alternative employment opportunities. Exhibit II shows a preliminary list of these series (with the number of federal workers in the series).

For the survey that will have to be conducted for the Professional and Administrative salary schedule, we believe it will be important to select benchmark jobs that are representative of the full range of series. It is obvious to us as both consultants and tax payers that the federal employees in these categories do not all have to be paid as though they are senior engineers, lawyers, or systems analysts.

It will require considerable planning to identify appropriate benchmarks, but this will be fundamentally important to the new survey's credibility.

While surveys could be conducted to collect market data for any series on this list, adding benchmark jobs increases the cost of the survey, and if data are relevant to only a small number of federal employees, at some point the added cost would be difficult to justify.

The selection of benchmarks for local surveys of Clerical, Technical and Other occupations represents a somewhat different problem. First, it is important that the benchmarks be proportionately balanced between clerical and technical occupations. Secondly, and more importantly, the benchmarks have to be the same for each local area. An option would be to limit the benchmarks for an area to the list of local federal positions. This, however, means that the survey results would vary from area to area as the mix of benchmarks changed. Similarly, if local employment levels are used as the weighing factors to combine survey data (i.e., the survey results for each GS level are calculated as weighted averages), it will make it difficult to compare the results across areas and also over time as shifting employment levels affect the results.

These prospective problems lead us to recommend that the benchmarks for the clerical and technical surveys be selected because it is reasonable to assume they will be found in the final universe of employers from which data will be collected. The weighing for each benchmark will be based on national federal employment levels. These decisions will be made without regard to local federal employment levels.

Our recommendations are consistent with a "market-sensitive" pay philosophy. The primary purpose is to have appropriate data to derive the federal "policy lines" from area to area. It is essential that the lines be comparable, and reflect only differences in local pay practices. Any aspect of the methodology that is affected by

changing local federal employment levels would introduce variability that we believe would be unacceptable.

- Salary Schedule Format

The rules used to design salary structures are, unfortunately, somewhat loose. There are no "right" answers, or universally followed practices. At the same time virtually all corporate salary structures conform to a general format.

There are four issues that need to be considered, with the answers to three essentially dictating the fourth. The basic issues are:

- salary range width or "spread"

This is the percentage difference from the range minimum to maximum. At the non-exempt level--clerical and technical positions--the typical corporate structure has a 40 percent spread. This increases at higher salary grades, with some corporations providing for a 60 to 70 percent spread at the executive level. Our recommendation to move to a 40 percent spread is conservative but consistent with our opinion of the step progression concept. Wider ranges would, of course, result in greater within-range variance, and the government would need a sound performance management program to justify the differences in individual pay levels.

- percentage difference between ranges

This is normally expressed as the percentage between midpoints. Corporate salary structures are based on a difference of perhaps 5 percent at the low end to 10 or more at the high end of current practice. For executive positions, the difference is sometimes as great as 15 percent.

- number of salary grades

It is impossible to compare salary structures on this issue because the numbers of grades is dependent, in part, on where the structure starts (the lowest range) and how high it goes. For the dollar range reflected in the General Schedule, it is safe to state that most corporations would have more than 18 grades. In concept, the number of grades should reflect the number of levels in the organization structure and job hierarchy. There is some interest in testing new structure concepts, but at this date there is no apparent trend to reduce the number of grades.

- planned range overlap

It is also impossible to summarize corporate practice on this issue. However, it should be apparent that increasing the number of grades or the range spread, or reducing the difference between midpoints, increases the degree of overlap.

There are compensation practitioners who feel strongly that a specific answer to one of these issues will enhance a salary program's effectiveness. However, there is no empirical evidence that these issues are more than causally related to a program's success or failure.

In light of the government's size and diversity of operations, we do not believe it is possible to argue that one schedule format would be better than another. We note, however, that the General Schedule, deviates from "standard" practice in the following ways:

- the range spread, 30 percent, is significantly less than the typical 40 to 50 percent;

- the difference between midpoints (Step 5), which ranges from 8.9 to 19.9 percent, is substantially above the norm; and
- the number of salary grades, 18, for the range of salaries, in theory from $10,213 (GS-1, Step 1) to $75,500, is at least five fewer than a typical corporate structure.

We recommend that the government "clean up" its structure by smoothing the percentage progression between the new midpoints (step 7). The current progression from one range to the next is irregular and exists for no apparent reason. While most of the differences are small and have no real significance, the schedule would appear more rational and be easier to explain to employees if the progression was constant. However, that will also affect the relationships which exist causing people to feel, in some cases, they have been disadvantaged. This could create controversy and therefore needs to be considered very carefully.

Currently, the grade-to-grade increase from GS-2 to GS-11 averages 11.3 percent, then suddenly increases 19.9 percent from GS-11 to -12. The average difference from GS-12 to -16 is 17.7 percent. The overall average, 13.7 percent, is approximately double the difference between grades that we would expect to see in a typical corporate salary structure for these salary levels.

At some point in the future, the government may want to modify the schedule at least above GS-11. If the midpoint-to-midpoint increase was a constant 12.0 percent, it would add two grades, as shown below. We also show the grade midpoints with an 8% progression. Our experience suggests that a change of this nature would make it easier to recognize and manage promotions.

Grade-to-Grade Progression

Step 7 Current		New/12%	New/8%
GS-11	$34,624	$34,624	$34,624
GS-12	41,498	38,779	37,394
GS-13	49,347	43,432	40,385
GS-14	58,312	48,644	43,616
GS-15	68,588	54,481	47,105
GS-16	78,869	61,019	50,873
--		68,341	54,943
--		76,542	59,338
--		--	64,085
--		--	69,213
--		--	74,750

In keeping with our recommendation to use step 7 as the midpoint range, it would make sense to smooth the step-to-step progression. We specifically recommend the following differences between steps:

	Step 1	Step 2	Step 3	Step 4	Step 5	Step 6	Step 7
Percent Increase	---	3.3%	3.2%	3.1%	3.0%	2.95%	2.85%
Illustrative Steps	$10,000	$10,333	$10,667	$11,000	$11,333	$11,667	$12,000
	|_____	_____	_____	20%	_____	_____	_____|

By using a constant dollar difference between steps, it produces a decreasing rate of increase. This is generally consistent with the learning curve concept that presumably applies to developing job skills.

- Use of Cost of Living Data

We strongly recommend that cost-of-living (COL) data be used only for determining payments made to employees at the time of an agency-initiated relocation. There are appreciable geographic differences in housing and other living costs, and, as an inducement to relocate, the government should reimburse employees for direct moving expenses and, if the new location is a high cost area, help employees with home financing.

Cost-of-living data is rarely used in the administration of white-collar salary programs. While increases in the COL indices are correlated with rates of increase in prevailing pay levels, they are driven by basically independent economic forces.

Pay increase rates or labor cost increases are dependent on the balance of the supply and demand for specific occupational skills, and this is the reason some occupational increase rates increase faster than others. Employers who rely on a market-based or market-sensitive compensation philosophy, adjust their salary programs periodically to keep the ranges properly aligned with prevailing rates.

The BLS Employment Cost Index (ECI) is constructed to be a time series index that tracks changes in labor costs. We have recommended the use of the ECI to adjust salary structures in years when surveys are not conducted. While it tracks labor cost increases for general, broad occupational groups, rather than specific job families, it should be sufficiently accurate for this purpose.

Our recommendation not to use measures of COL changes are based on the following concerns.

- The government's objective should be to maintain a competitive salary program, not to guarantee that its employees will be unaffected by changes in living costs. This is an important philosophical point.

- There is not, and cannot be, a single index that represents the increase in living costs for all employees. There are simply too many factors that affect an individual family's living costs, the most important of which is his or her income. This is the reason the BLS carefully defines the assumed family structure in developing its COL indices.

- Living cost increases are not always identical to labor cost increases. For example, when the rate of inflation was at its peak a decade or so ago, the annualized rate for some months exceeded 15%. Salary increase budgets during this period never exceeded the 10% level. More recently, salary budgets have been in the 5-6 percent range, while inflation has been in the 4 percent or less range (until the past year). If federal salaries were tied to COL increases, the former situation would undoubtedly be unacceptable to Congress and the latter unacceptable to federal employees.

- It is theoretically incorrect to argue that a valid single COL index can be derived for a major metropolitan area. The differences in housing costs and in local tax rates across areas like New York and Los Angeles are substantial. In fact, it may be correct to state that the intra-region differences are often greater than the inter-region differences. Any attempt to develop a single index has to be based on assumptions about where federal employees live or where they should live. This would be difficult to defend.

- Finally, comparative COL data that meets the usual BLS validity standards are unavailable. The BLS discontinued a series of reports referred to as Family Budget Studies in the early 1980's. It is our understanding that this action was taken because the assumptions about how families spend money were no longer valid, and that it would have cost too much to update the studies. Comparable data is unavailable at this time.

While corporations certainly consider COL increases in establishing their salary increase budgets, and in some cases continue COL increase provisions in their labor contracts, they do not use these data in mechanistic formulas to adjust their salary programs.

- Problems with the Classification System

There are serious, widely acknowledged problems with the classification system. There is a general consensus that it is "broken," and needs to be modernized. While a new "start from scratch" system would be advantageous, it would be unrealistic to initiate this additional work at this time. Even if the objective is to replicate existing salary grades under a new classification/job evaluation method, the new system will inevitably indicate that new grades are needed for some jobs. The turmoil that this will trigger could easily derail the effort to gain agreement on the other changes in the salary program.

At the same time, the problems with the classification system are too pervasive to "clean up." It is unreasonable to expect all the employees in positions that are overgraded to accept a reduction in grade before the salary schedules are adjusted to be in line with the market, and conversely it is unreasonable to seek schedule adjustments until jobs are in the "correct" grades. There is no easy answer to this problem, and we recommend that OPM be delegated the flexibility to work with the key players to develop a viable and equitable solution.

At some point, Congress should consider whether the job hierarchy established by Title 5 is still appropriate. It may, at that time, be useful to consider if it is still necessary and in the government's interest to have a statutorily-defined job hierarchy (i.e., at present the levels of work which constitute a grade are specifically defined in the law). This obviously makes it more difficult to respond to labor market trends.

Our recommendation to split the General Schedule, and to establish new schedules for occupations that do not fit the white-collar concept could also strengthen the argument to revise the system. Most recently-developed job evaluation systems are based on so-called "compensable factors." The government's Factor Evaluation System (FES) uses nine factors. In concept, the factors should be based on the organization's value system, and be relevant determinants or measures of job value for the positions covered under the system. There has been an ongoing concern that (1) all of the FES factors are not necessary and (2) the factors are not valid or credible for some occupations.

If new salary programs are created for health care specialists and for the law enforcement series, it will be advantageous to establish new job evaluation systems that are specific to each group. With law enforcement positions, for example, factors such as "Responsibility for the Safety of Others" and "Personal Risk" may be appropriate. With health care specialists, a factor such as "Responsibility for Patient Care" might be appropriate. With these occupations out of the GS program, it may be reasonable to consider reducing the number of factors used in FES.

In the past few years, the concepts and methods used in job evaluation have begun to shift from the manual, labor-intensive approaches used for the past three or four decades to automated systems based on rigorous analytical techniques. The new approaches take advantage of relatively recent developments in information management, more precise and valid measurement concepts, and artificial intelligence decision techniques.

We estimate, conservatively, that the government is currently spending over $200 million a year to maintain the classification system. This is based on the number of employees in series 221, and their average salaries. The total is also based on assumptions regarding the cost of benefits, support staff salaries and their benefits, supervisory time, and office space and equipment costs. If the government's classification function were to be converted to a more modern approach, taking

advantage of recent developments that make it possible to automate some of this work, there could be significant cost savings.

The new approaches are faster and more efficient and, perhaps more importantly, represent more effective management systems. If the government decides to change its classification system, it will be important to base a new system on better methodologies.

- Recruiting and Retention Bonuses

Lump-sum bonus payments are common in executive recruiting and used occasionally for recruiting lower-level professionals. This practice is generally identified with more aggressive corporations who are recruiting the "best and the brightest." With individuals who are employed, the bonus payments are intended as an inducement to leave what is presumably a solid, attractive career opportunity for what is essentially an unknown, somewhat risky new situation. Unfortunately, we are not aware of any recent surveys on this issue.

Retention bonuses, on the other hand, are relatively uncommon, or perhaps more accurately, corporations do not make payments that are referred to by this name. In fact, many employers make year-end incentive payments, where the amounts are dependent on corporate and/or individual performance. Since individuals who terminate during the year lose the money, the unstated objective of these programs is to provide an incentive for participants to stay at least through year-end.

(We are aware that the armed services have used bonus payments, but we suspect that the career decisions in these situations are not typical of white-collar college graduates.)

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We have not recommended that the government move to a recruiting or retention bonus program because in our opinion these practices make sense only if it proves to be impossible to make the pay program fully competitive. The need for both recruiting and retention bonuses is symptomatic of deficiencies in the basic salary program. If the salary program were competitive, bonus payments would not be necessary. Despite this perspective, we fully appreciate that until the program is competitive, limited use of bonus payments may serve the intended purpose, and we recognize the cost/benefit value of both recruiting and retention bonus payments.

In recruiting most of the government's new hires in professional and administrative positions are recent college graduates. For these individuals, government service represents a different career path, and frankly is one that is currently attractive to a limited group of graduates. Higher salaries would enhance the image of government careers and presumably increase the pool of applicants; however, starting salary is only one factor in considering career alternatives and there are other factors that have contributed to the government's poor image as an employer.

As a "tool" available to recruiters, recruitment bonuses would presumably be helpful with some applicants. However, not every applicant warrants a bonus to accept a job offer, and the government should take care in administering such a program to ensure that it does not become automatic.

An issue, of course, is that bonuses can be paid only to individuals who have expressed an interest in a government career. We are aware that there have been recent efforts to make government recruiting more proactive and aggressive, which may increase the level of interest in government careers. As part of an aggressive recruiting program, the possibility of bonus payments could be useful, but the government has fundamental problems to correct if it wants to recruit high calibre prospects.

On the retention side, we are even less convinced that bonus payments would be effective. This is not like re-enlisting in an armed service. Realistically, even corporations with year-end bonus programs know that once the payment is made, the "golden handcuff" is unlocked. The bonus payments may only postpone a decision made earlier in the year. Moreover, it is also true that outstanding performers, presumably the individuals the government wants to keep, can always get more cash from a new employer to make-up for any bonus they would have to forfeit. Our experience suggests that career-oriented, employees decide to change employers when they become convinced that their current employer is no longer offering them an adequate career opportunity. Retention bonuses alone will not change an employee's view of government careers--at least for those employees who can find other opportunities.

Despite our concern about the effectiveness of recruiting and retention bonuses, we appreciate that they will serve a purpose if the program is not modified to be more competitive. Recruiting and retention bonuses might serve a useful purpose during the phase-in period. If other recommendations are not fully adopted, it will be advantageous to authorize bonus awards to help the departments and agencies overcome the deficiencies in the program.

- Dual Career Ladders

We believe the government should study its promotional and career planning practices to determine if the dual career ladder concept would enhance employee career prospects. The government has a large number of senior "experts" who are at the top of their respective career ladders. For many of these individuals, the available career step is to move away from "what they do best" and become supervisors. The skills that made them technical experts are different from those needed to be a supervisor or manager, so there is no certainty that they will be successful in the new position.

The dual career ladder concept would make it possible for the senior experts to move up another step or two, and possibly to earn as much or more than the individuals supervising the staff. The concept has been used successfully with scientific and engineering staffs. The government has other professional career ladders where technical expertise is similarly important. In fact, many of these experts are at the top of their professions. In promoting these individuals to supervisory positions the government is losing some degree of this expertise.

As consultants, we have been exposed to this problem in professional service firms. Lawyers, actuaries, accountants and stock brokers all depend on individual expertise which is lost when an individual is promoted to a supervisory position. Quite often the individual is less satisfied in the new position.

It may be that expanding the professional career ladders, with increased compensation opportunities, would help the government avoid losing this valuable resource.

- Salary Increases and Pension Benefits

The Civil Service Retirement System (CSRS) and the Federal Employee Retirement System (FERS) are based on the same logic as the typical corporate pension plan--pension benefits are calculated with a formula that takes into account years of service and compensation levels prior to retirement. The level of pension income is planned using a replacement-ratio concept so that the employee's pension income is related to his or her pre-retirement compensation. With FERS, of course, retirement income also includes Social Security and amounts attributable to accumulated thrift plan savings.

In keeping with this philosophy, we recommend that any increase in salaries be reflected, as the retirement plan formula provides, in pension benefits. The only argument against this is cost.

A geographic differential paid to professionals and administrative personnel in New York, Los Angeles and San Francisco, for example, should not be considered or treated for pension purposes as base salary. We do, however, recommend that it be added to the pension calculation if the employee works in one of these areas for the five (5) years prior to his/her retirement. An employee's pension benefit should not be affected, either increased or decreased, if he/she is asked to relocate for a brief period immediately prior to retirement.

For the period when an employee works in an area with a geographic differential, the normal pension contribution should be deducted from the differential. If the employee relocates to an area where he or she is not eligible for a differential, the aggregate contributions deducted from the differential, with reasonable interest appreciation, should be returned as a lump-sum payment. The geographic differentials should also be taken into account in determining the amounts employees can contribute to the thrift plan.

When employees retire, they typically continue to live in or close to the area where they worked. For those individuals who relocate after retirement to a new residential area, such as Florida, it is a personal decision and the government cannot, and should not try to take these decisions into account in planning its pension, program. If the individual plans for the relocation far enough in advance, the thrift plan should make it possible to accumulate additional assets.

- Relocation and Mortgage Differentials

In addition to the recommended salary differential for the four geographic areas initially identified as high cost, we recommend that the government provide financial assistance to enable relocating employees to purchase a home. Real estate prices in all four areas are significantly above national norms, and our experience suggests this problem heightens the interest in cost-of-living and/or salary differentials. It is, of course, true that other areas across the country have relatively

high real estate prices. If the government wants an employee to disrupt his/her life and that of his/her family and relocate, it is important that the government make it financially possible to do so without adversely affecting the employee's life style.

At the same time, of course, federal workers who already reside in areas with high real estate prices have developed a personal "solution" to the problem. Although they may have aspirations to purchase a more expensive property, their goals are shared by thousands of other residents who cannot afford the home of their dreams. The government has no reason to assist these federal workers.

In fact, we would argue that the government should be careful to avoid any policies or practices that would treat its employees better than other residents of the area working in comparable jobs. Our recommendations for geographic salary differentials are intended to place federal employees on a par with other workers in comparable jobs, but the government should not feel any obligation to go beyond this for employees who already reside in the area. We strongly recommend against any concept that essentially "guarantees" that federal workers in these areas will be protected against future cost-of-living increases when voters in the areas do not have similar protection.

Employees who are being relocated, however, do need assistance. The typical corporate relocation policy provides for reimbursement of virtually all direct expenses associated with the move. It is our understanding that government policy provides for reimbursement of most expenses, including closing costs, moving household possessions, house hunting trips and limited temporary living costs.

It is housing that is a continuing problem, and perhaps the one that is the most sensitive to public scrutiny. There are two issues: securing the down payment required for "adequate" housing, and paying the monthly costs (mortgage and local real estate taxes). The government should commit to both types of assistance. Our

recommended approach is comparable, although somewhat more precise, than the typical corporate practice.

A basic issue is the relative value of housing in the area where the employee currently resides, and values within commuting distance of the new work location. The most widely used source of this information is Runzheimer International. Although the government would need to confirm the relative validity of these data, we recommend that the government rely on this firm, unless BLS has access to better data.

It is reasonable to assume that the relocating employee should be able to live in a "comparable" neighborhood, although we appreciate that this may not be realistic in one of the extremely high housing cost areas. When we met with the New York FEB group, for example, they provided a map of the area with concentric rings showing relative housing costs as one moves away from New York City. The situation in Los Angeles is similar. These may be extremes, but the problem is the same for every resident of these areas, which is the reason many workers tolerate long commutes. From our perspective, it would be reasonable to adopt a policy that employees should not be expected to live more than 50 miles from their work location.

The relevant comparison then is the comparative value of the employee's current residence and that of a "comparable" residence in the new area. If the new area is higher, the government should commit to:

- a lump sum amount equal to the difference between 20 percent of the "average" value of a comparable home in the new area and the employee's equity in his/her current property, subject to a maximum of three month's salary, and

- a monthly mortgage differential payable for three years based on the difference between the mortgage payment assuming the employee purchased an "average" home and used his/her equity (plus the lump sum payment, if any) as the down payment, and his/her current mortgage payment, subject to an annual maximum of $5,000 (adjusted annually by the change in home ownership costs).

In computing the monthly mortgage differential, we recommend that anticipated real estate taxes (adjusted for the federal tax effect) be included in the calculations for both the new and old residence. In some areas, such as several suburbs around New York, real estate taxes are substantially higher than the national "norm."

We believe this approach is reasonable. The aggregate amounts for the typical move are roughly consistent with the FBI's new policy for New York. It would be virtually impossible to develop a sensible lump-sum approach applicable to all federal relocations, so we specifically recommend that the government avoid lump-sum payments for relocation to other areas.

RESPONSES TO SUPPLEMENTAL OPM QUESTIONS

1. Is it possible or desirable to continue a national pay schedule for any jobs currently covered by the General Schedule?

It is certainly possible but definitely undesirable to maintain a national schedule for any jobs without the inclusion of appropriate geographic pay differentials. Realistically, geographic pay differentials exist for all occupations. A pay schedule that is "competitive" in New York or Los Angeles would result in salaries that are significantly above the market in most other areas. Conversely, if a schedule is in line with prevailing rates in rural areas, it may be impossible to hire workers in New York or Los Angeles. Neither situation is acceptable.

Our recommendation to establish local salary programs for Clerical, Technical and Other series is consistent with generally accepted views of the labor markets relevant to these positions. Workers are recruited and hired from a relatively small geographic area around a work location. The government needs to maintain a salary program that is competitive within this area.

For the Professional and Administrative series, we have recommended geographic salary differentials for a limited number of locations. These are widely recognized by other employers as problem areas that warrant special personnel policies.

The survey data for these occupations show geographic differences for other areas, but our experience suggests that some of this is "noise" in the data. There is an error factor in all survey data so we do not want to place too much emphasis on small variations in survey results.

The labor markets for these occupations also tend to be larger and more regional in nature. Although our database is limited to major metropolitan areas,

we would not expect significant decreases in prevailing rates for non-urban areas. As our corporate surveys show, employers generally use national salary structures so that within a corporation salaries for similar jobs will be consistent across their area of operation. Moreover, the organizations both recruit for these positions on at least a regional basis and occasionally relocate these employees from one area to another. In other words, these occupations are managed on the basis of broader regional or national labor markets.

The personnel problems associated with New York, Los Angeles, and San Francisco are more related to relocation and housing costs than to differences in salary. While we are recommending salary differentials, we have considered the housing problem in our recommendations related to the government's relocation policies.

To reiterate, we do not believe maintaining a national salary schedule without the flexibility for geographic "add ons" is practical.

2. Propose alternatives to the General Schedule with specific treatment of:

- Occupations and grade levels, and groupings or categories of occupations

Our recommendation to establish local salary programs for clerical/technical employees is based on two fundamental assumptions:

- the Title 5 job hierarchy and the classification system cannot be completely discarded; and
- it is important to keep the program as simple as possible.

Our recommendations are also consistent with the private sector model. While it would be possible to develop more complex but theoretically sound program

concepts, the fact is that the basic private sector approach works, employees can understand it, and it is generally accepted.

With computers, it would be possible to establish and maintain separate salary programs for numerous combinations of series. This would place a much heavier emphasis on surveys to determine competitive pay levels for as many series as possible. This would, however, quickly grow into a monstrous and unnecessary bureaucracy.

Some individuals have argued that the local pay programs should be based on grade levels. For example, all employees at GS-7 and below would be paid on a local basis. However, this approach at any level introduces breaks in occupational career ladders. In moving from local to national schedules, these breaks would inevitably result in unwarranted large promotional increases, or result in pay reductions, depending on how the local and national schedules interface. This makes this alternative unworkable.

If the basic General Schedule program cannot be modified, we recommend the expansion of the special rate provisions. However, we would note that there is a fundamental flaw in the current special rates program. The law requires that there be a demonstrated problem of recruitment and retention before its provisions are operational. This can result in the loss of the most marketable individuals, who may be critical to an agency's mission, before rates can be raised to more closely reflect the market. Regardless of other changes, this provision should be changed to ensure that agencies are able to adjust to anomalies in the market before a serious recruitment or retention problems develops.

Care must be taken to ensure that within the same location, agencies are not individually "ratcheting-up" pay rates, thus, creating a bidding war for the same labor pool within a community. This situation would place agencies with severe budget

constraints at a significant disadvantage and would be considered unacceptable by taxpayers.

Of course, as salary structures become increasingly competitive, the need for special rates should become the rare exception. In any case, OPM should develop policies to ensure a balanced approach.

- the relationships and/or linkages among the schedules;

The relationships between the local salary schedules under our recommendation would in direct terms be nonexistent. Each schedule would be free to move up or down as dictated by prevailing market rates. Indirectly, the schedules will be based on the same benchmark jobs, the same survey methodology and the same administrative mechanisms. This will result in a high degree of consistency from area to area.

- how workers could move within and among schedules;

Movement within a schedule will be the same as it is under current practice. Movement from one local area to another for clerical/technical employees is rare, and normally not initiated by the government. The only movement that has surfaced in our meetings is prompted by spouse relocations, and we recommend that the government accommodate the affected employees, assuming they are satisfactory performers, with a lateral transfer at the salary paid at the new locations.

There will be situations when an employee changes career paths, and is promoted from a clerical/technical position to a professional or administrative position. It is impossible to foresee all the scenarios that may occur. This, of course, occurs in corporations as well, and it is generally not a problem. OPM should develop pay administration policies which allow for a reasonable transition and salary progression.

Professional and administrative employees moving from the national schedule rates to one of the areas with salary differentials would be paid the appropriate salary for the new position, plus the differential. If they move away from the high pay area, they will lose the differential. This is simple and straightforward, and we do not foresee any problems. The scattered data available suggests that less than 5 percent of the employees in these occupations are relocated each year.

- rate range widths;

We recommend 40 percent salary ranges. The current 30 percent is significantly less than prevailing practice. While corporations commonly have ranges that exceed 40 percent, this makes sense in our opinion only with a meaningful pay-for performance program. The range width also governs the variance from the midpoint, and if the range is set properly relative to market pay levels, the width governs salaries relative to the market. From our perspective, it would be a mistake to adopt a range width that permitted salaries to move too far above market.

- and alternative methodologies for adjusting schedules, differentials, etc.

In our professional opinion, the only alternative for adjusting schedules is the movement in market pay levels. This is fundamental with a market-sensitive pay program.

We a aware that some individuals have advocated the use of cost-of-living increase rates but for the reasons discussed previously, we are opposed to this alternative.

3. Should geographic differentials be a part of the system?

- If so, how should they be determined?

We are recommending salary differentials at this time for professional and administrative employees in these three areas: New York and its environs, Los Angeles, and San Francisco

We recommend that the differentials be calculated by comparing the national "policy line" with separate reference lines computed for each location. This approach will make it possible to calculate a separate percentage differential at each GS grade. The survey data suggest that (a) the reference lines at each location are above the federal policy line and (b) the slope of the lines vary by grade.

- Under what circumstances should they be applied?

The differentials should be paid to all professional and administrative employees in these locations.

The housing allowance, where applicable, will be paid only to employees who relocate and it should terminate after three years.

- Should differentials be paid as part of the base salary or as a separate payment?

All differentials should be handled as separate payments.

4. If local or regional schedules or differentials are recommended, how should these schedules be constructed?

We recommend that the schedules be constructed using essentially the methodology currently used with the General Schedule.

After the survey data is collected and summarized, the average (preferably median) market rates for the positions assigned to each grade will be aggregated into a salary grade average (using national federal employment in each position as the weighing factor).

These results will be used to compute a so-called "policy line." Regression techniques help to generate a smooth line of "least squares," based on the aggregated survey results.

The midpoint (Step 7) of each grade would be calculated by using the policy line derived for each area. Minimums and maximums are then determined using the midpoints and the recommended 40 percent range spread.

This approach is consistent with accepted practice within the compensation field.

5. Should schedules be developed individually for each local area?

- Should a limited number of schedules be used and cities/MSA's/other designated areas be assigned to one of these basic schedules?

We initially considered but rejected this approach because it has inherent political problems. It is probably valid to assume that no more than five to seven schedules would suffice for the entire country. However, as local labor markets move up or down over time, we anticipate that there would be intense pressure to assign an area to the next highest (or lowest) schedule. In light of the error factor in survey data, it would be hard to defend such decisions. If the employee unions become involved (as with PRAC), the negotiations needed to resolve disputes could be disruptive.

The alternative is the FWS model, where salary schedules are independently derived for each area. Here the schedules are essentially free to "float" with the survey results. This approach seems to be well accepted by both labor and management in the FWS administration. We believe it would work well with the clerical/technical salary program.

- Should the General Schedule be continued as a base schedule with differentials?

Any decision to continue the General Schedule would have to assume that the salary levels are "correct" for some occupations or locations. There are no data to support this assumption. The number of grades and pay rates have little relevance once the clerical/technical, law enforcement and medical specialty occupations are removed.

The salary program needs a new foundation. While we have recommended continued use of the General Schedule format, we are not convinced that the GS salary ranges are appropriate for any future purpose.

- How should schedules/rates be determined when few, if any, job matches exist in a local area?

We have recommended the use of a constant set of benchmark positions, regardless of local job matches. If this were to be a "market-based" pay program, this would, of course, be essential. However, the purpose in using the survey data is to derive a policy line that is consistent with the local market data. Individual positions are assigned to the structure based on the classification process.

This obviously minimizes the importance of local job matches. Any methodology built around local job matches would introduce variance that is attributable to sampling differences. In some areas the "high pay" jobs may be

present; in others the "low pay" jobs may dominate. The recommended approach would, in concept, limit the source of variance to local salary differentials.

6. How do these recommendations compare and contrast with generally accepted public and private sector systems?

Our recommendations are based solidly on established private sector practice. Realistically, no corporation or, for that matter, no state government has to deal with a compensation problem that is as complex as that of the federal government. Our recommendations often involve refinements of established practice.

One of the differences is the use of salary differentials. While many employers, including the government, routinely use separate differentials in conjunction with expatriate salary programs, it is relatively rare to find differentials used for U.S.-based employees. Within the private sector, differentials are sometimes used to cover relocation expenses, especially housing in high cost areas, but corporations would commonly cover geographic salary differences simply by paying higher salaries.

EXHIBITS

BENCHMARK OCCUPATIONS USED IN PATC SURVEY

PROFESSIONAL OCCUPATIONS

- Chief Accountants
- Public Accountants
- Auditors
- Attorneys
- Chemists
- Engineers
- Registered Nurses

ADMINISTRATIVE OCCUPATIONS

- Personnel Specialists
- Personnel Supervisor/Managers
- Directors of Personnel
- Buyers
- Computer Programmers
- Systems Analysts
- Systems Supervisors/Managers

TECHNICIAN OCCUPATIONS

- Nursing Assistants
- Licensed Practical Nurses
- Civil Engineering Technicians
- Engineering Technicians
- Drafters
- Medical Machine Operators
- Computer Operators
- Photographers

CLERICAL OCCUPATIONS

- Accounting Clerks
- File Clerks
- Key Entry Operators
- Messengers
- Personnel Clerks/Assistants
- Purchasing Clerks/Assistants
- Secretaries
- Stenographers
- Typists
- General Clerks

Exhibit II

POSSIBLE BENCHMARK FEDERAL SERIES

Job Series		Federal Work Force
318	Secretary	91,545
334	Computer Specialist	40,119
322	Clerk-Typist	39,743
2005	Supply Clerical & Technical	28,081
855	Electronics Engineer	24,389
802	Engineering Technician	22,167
305	Mail and File Clerk	21,492
525	Accounting Technician	20,580
856	Electronics Technician	19,877
810	Civil Engineering	15,579
905	General Attorney	13,725
356	Data Transcriber	13,714
830	Mechanical Engineering	12,434
998	Claims Clerical	11,670
203	Personnel Clerical & Assistant	11,444
560	Budget Analysis	11,260
510	Accounting	10,210
2010	Inventory Management	9,528
335	Computer Clerk & Assistant	9,520
1106	Procurement Clerical & Assistant	9,512
332	Computer Operation	9,469
201	Personnel Management	8,779
511	Auditing	8,704
861	Aerospace Engineering	8,300
1712	Training Instructor	7,189
1320	Chemistry	6,525
1105	Purchasing	5,979
850	Electrical Engineering	4,402
110	Economist	3,977
1165	Loan Specialist	3,973
544	Payroll	8,897
212	Personnel Staffing	3,869

POSSIBLE BENCHMARK FEDERAL SERIES

Job Series		Federal Work Force
1515	Operations Research	3,591
561	Budget Clerical & Assistant	3,464
1310	Physics	3,352
896	Industrial Engineering	3,009
2134	Shipment Clerical & Assistance	2,784
1520	Mathematics	2,574
950	Paralegal Specialist	2,437
235	Employee Development	2,382
1350	Geology	2,311
382	Telephone Operating	2,217
1530	Statistician	2,212
1340	Meteorology	2,114
1411	Librarian Technician	2,082
1410	Librarian	1,988
840	Nuclear Engineering	1,916
1550	Computer Science	1,877
230	Employee Relations	1,776
808	Architecture	1,754
2091	Sales Store Clerical	1,654
403	Microbiology	1,534
505	Financial Management	1,295
818	Engineering Drafting	1,191
1654	Printing Management	1,049
233	Labor Relations	1,029
1640	Facility Management	891
304	Information Receptionist	872
2030	Distribution Facilities & Storage Management	791
1176	Building Management	779
1160	Financial Analysis	727
1360	Oceanography	688
414	Entomology	683
170	History	599

POSSIBLE BENCHMARK FEDERAL SERIES

Job Series		Federal Work Force
807	Landscape Architecture	559
1016	Museum Specialist and Technician	553
1373	Land Surveying	501
1040	Language Specialist	472
881	Petroleum Engineering	470
193	Archeology	468
1330	Astronomy & Space Science	457
880	Mining Engineering	419
408	Ecology	320
1321	Metallurgy	319
405	Pharmacology	299
471	Agronomy	298
1015	Museum Curator	297
302	Messenger	257
150	Geography	204
430	Botany	147
1510	Actuary	122
437	Horticulture	110
385	Teletypist	101
410	Zoology	100
184	Sociology	62

STUDY OF FEDERAL EMPLOYEE LOCALITY PAY

TASK 5: *Designing, Modifying And Costing Of Locality Pay Systems*

TASK 5 - DESIGNING, MODIFYING AND COSTING OF LOCALITY PAY SYSTEMS

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APPROACH TO THIS TASK

The objectives of this Task are to use our analyses and recommended program changes to estimate the cost to adopt the new program and to comment on some of the issues related to the implementation of the new program. The primary consideration is the methodology used to estimate the costs. We believe our methodology is logical in light of the government's normal approach used to determine the annual adjustment to the General Schedule and is also consistent with widely used concepts to develop new salary structures.

METHODOLOGY TO ESTIMATE AGGREGATE COST TO IMPLEMENT RECOMMENDATIONS

The methodology is designed to estimate the aggregate cost to the government to implement the following recommended program changes as of October 1, 1989:

- local salary schedules for Clerical, Technical and Other series employees for the 48 metropolitan statistical areas (MSA's) in the OPM database; and

- a national salary schedule for Professional and Administrative series employees in the same MSA's, with additional salary differentials paid to employees in the New York and its environs, Los Angeles, San Francisco and possibly including Boston and Washington, D.C. MSA's.

We want to point out that our recommendation is to consider geographic salary differentials for professional and administrative employees in New York and its environs. The survey database covers only the New York MSA, so more extensive surveys will be necessary to confirm prevailing pay levels between these metropolitan areas.

For the benchmark jobs, it is a straightforward calculation to determine the difference between private and federal salary levels. The "cost" to bring federal salaries in line with private sector salaries is simply the difference in dollars multiplied by the number of federal workers in each job.

The problem is that the incumbents in benchmark jobs represent roughly 30 percent of the federal work force. The database is most extensive in Washington where the benchmarks account for 41.7 percent of the work force. The "constructed" data account for 50 to 60 percent of the work force across the metropolitan areas, but these data are somewhat less defensible than the actual survey data. There is

a need, therefore, for a methodology that estimates the salary adjustments needed across all series, grade levels and locations.

The methodology developed for this purpose is based on the "policy line" concept that has been used in the compensation field for several decades. It normally serves as the basis for developing a new salary structure using salary survey data. A policy line goes through the market averages and is used to determine the midpoints. This is somewhat similar to the methodology followed by OPM in which PATC survey data is used to adjust the General Schedule. In effect, we used the survey data for each MSA to develop what would become a separate salary schedule based on the prevailing pay rates for the area. The cost estimate for the MSA is based on the assumption that the salaries for the employees in the area were adjusted to the appropriate steps in the new GS ranges, based on the local market rates.

To develop the policy lines, we used linear regression techniques to determine the line of best fit between the respective salary survey mean values (the "Y" or dependent values) and the Factor Evaluation System (FES) point totals (the "X" or independent values)[1]. Separate lines were developed for Clerical/Technical positions and for Administrative/Professional positions.

In using the FES points, we are assuming that the government will continue to use the title 5 job hierarchy and the classification (actually FES) system. Although there is, naturally, variation in the survey means around the private sector lines, the regression line provides the "best" pay level estimate for a job once FES is applied to determine its relative value in the government's job hierarchy. The

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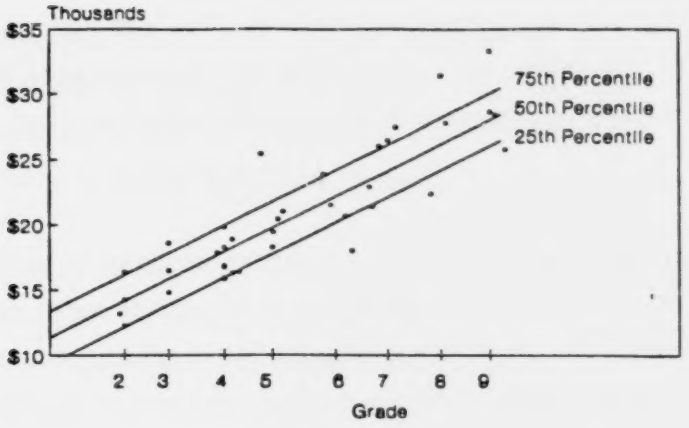
[1]In some MSA's, curvilinear lines would have "fit" the data better but (1) it is important to be able to compare across MSA's, (2) linear policy lines have been traditionally used in the private sector, (3) the linear concept is consistent with the premise that each FES point has a fixed value, and (4) curvilinear equations are more difficult to understand.

points on the line effectively balance the labor market's hierarchy, as reflected in the survey data, with the government's hierarchy. The market may pay more or less for a given job but the line provides "answers" that are consistent with the government's concept of internal equity, as reflected in the FES point totals.

The following graph illustrates the concept of a policy line.

Determining a Policy Line
from Survey Data



Although FES has not been applied to all job series, we were able to identify a sufficient number of benchmark jobs, by GS grade and series, for which FES point totals were available. For jobs where FES point totals are unavailable, we made the assumption that the point totals for the jobs would be equal to the average for other benchmark jobs at the same GS grade level. The actual number of benchmark jobs used in each MSA to construct the policy lines varied with the number of benchmark matches for the MSA. Our review of the equations suggests that the results are generally in line with our understanding of the labor markets, and our analysis of the OPM database.

The national line for the Administrative and Professional series was based on an analysis of actual survey data for MSA's across the country. New York and its environs, Los Angeles and San Francisco were excluded because a special differential is recommended for these areas. If these areas had been included in the national line calculations, the line would have been elevated and would overstate the market pay levels for the other 45 areas.

To estimate the difference in pay for a job specified by series and GS level (e.g., a GS-9 computer specialist), the sequence of steps is as follows:

1. Once we have the FES points, we can use the points with the relevant private sector line (or equation) to estimate the market rate for the job in the MSA. For those jobs where survey data is unavailable, this is our best estimate of what the local market would pay the job. We can estimate a "market" rate for any job, even those that are unique to the federal government.

2. By subtracting the actual federal mean salary from the estimated market rate, we have an estimate of the difference between the private sector market means and the current federal mean.

3. The difference is then multiplied by the number of federal incumbents to give us an aggregate estimate of the cost to adjust salaries for the job to private sector levels.

4. By aggregating across jobs at each GS grade level, and then across the 15 GS levels, we can estimate the aggregate cost to bring federal salaries in line with the private sector for a given MSA.

It is important to note that since we started with the assumption that no federal employee will have his or her salary cut, at grades and locations where federal salaries were found to exceed private sector salaries, the negative values were

ignored in developing the total costs for an MSA. (If salaries were to be cut, these savings could be used to reduce the cost for an MSA.)

It should be noted that our conclusions are tentative and, as such, will require additional surveys, designed to include local and state governments in the database. We anticipate that the additional surveys will be useful in fine-tuning the cost estimates and will support our conclusions.

The advantages of this methodology are:

- it is relatively straightforward and conceptually simple;
- the results are explainable and defensible;
- it is generally consistent with the approach used by private sector employers to link salary structures to market-dictated salary rates;
- it is based on widely used techniques;
- it treats all series and locations on a consistent basis; and
- the conceptual logic can be used in the actual development of the new salary schedules.

The national line for Administrative and Professional employees could be used to estimate the salary gap for individuals based outside the 48 MSA's. Although data for these individuals are not included in the OPM database, the data are available in the Central Personnel Data File. The estimation process is straightforward and simple. For the remaining Clerical and Technical employees, none of the metropolitan area policy lines is directly relevant. However, based on our experience and the anticipated urban/nonurban differential, we "guesstimate" that the salary gap is less than 10%.

ESTIMATED AGGREGATE COSTS

The aggregate costs to implement the recommendations in the 48 MSA's depend on the policy the government adopts in aligning its salary levels relative to the market. This issue is further discussed in the next section. The aggregate costs shown below are based on the assumption that the government will align the midpoint or 50th percentile of the General Schedule at each grade with average private sector pay. Other policy options would produce different results.

	Professional/ Administrative	Clerical/ Technical and Other	Total
Necessary Increases As of October 1, 1989	$2.381B	$1.058B	$3.439B

For the purpose of this study, we have updated the estimates to October 1, 1989. OPM has informed us that federal salaries were increased by 4.1 percent in January 1989. In the private sector white-collar salaries are currently increasing at an approximate annual rate of 5.0 percent. From March 31, 1988 to October 1, 1989 is a period of 18 months; therefore, it is reasonable to assume that private sector salaries would be 7.5 percent higher (5.0 x 1.5) than in the OPM database. Our calculation takes into account both the estimated change in private sector salaries and the 4.1 percent increase in federal salaries.

The individual MSA cost estimates are summarized in Exhibit I.

If additional geographic salary differentials were paid to the Professional and Administrative employees in New York and its environs, Los Angeles and San Francisco, we estimate that the aggregate amount would be $137M as of October 1, 1989. This is based on the difference between the local policy lines calculated with

local survey data for each city and the national policy line.[2] If geographic differentials were paid to Professional and Administrative employees in Boston and Washington, D.C., the cost would be higher.

Adding the estimates of the salary differentials for the three metropolitan areas to the aggregate cost of the national salary adjustment produces an overall cost estimate of $3.576B to implement the recommended program changes.

It is important to emphasize that these estimates are based on survey data that is recognized to be imperfect. New surveys, which will need to cover the non-urban areas and state and local government jobs, are necessary to confirm and refine the estimates. It also would be advantageous to address the over grading problem as further refinement of the estimates.

With the 4.1 percent increase (January 1989), the annualized aggregate payroll for the federal employees included in the database is $23.852B. The necessary increases including the salary differentials, therefore, represent a 15.0 percent adjustment.

The total white-collar payroll, as of March 1, 1988, was $41.6B. Of this amount, $18.7B was paid to workers based outside of the 48 MSA's. The necessary adjustments for this group of positions should be in the $2.4B to $2.8B range. We estimate that the total increase for employees covered under the current General Schedule would be approximately $6.B or 14%. (Survey data are unavailable to develop more precise estimates.)

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[2]For these cities, separate regression lines were calculated using the local survey data, and used to estimate aggregate payroll costs if the federal program was adjusted to be competitive in each city. These cost estimates were compared with the estimates based on the national policy line. The aggregate salary differential is the difference in payroll cost above the national line for the federal program to be comparable to prevailing local salary levels.

This percentage compares with an estimated gap of 27.0 percent based on PATC survey data[3] and the government's normal method for comparing the General Schedule and average federal salaries to private sector salaries. Using the PATC estimates the cost to close the gap would be $11.7B.

AGGREGATE COST COMPARISONS OF TWO METHODS
WYATT MARKET-BASED AND PATC
(In Billions of Dollars)

WYATT COST ESTIMATES
FOR 1989

	48 MSA Professional Administrative	48 MSA Clerical/ Technical	Other Locations	Total WYATT	Estimated 1989 PATC
Adjustment	2.381	1.058	2.424	5.863	---
Differential LA-NY-SF	.137	---	---	.137	---
Total Dollar GAP	2.518	1.058	2.424	6.000	11.7
Total Percent GAP	___	---	---	14%	27.0%

As can be seen in the table above, the combined cost of the Wyatt recommendation based on adjusting Federal salaries to the market lines at the 50th percentile is $6 billion. This contrasts sharply with the $11.7 billion cost estimate derived under the PATC methodology. (While we understand the limitations of the

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[3]Because a revised PATC survey report was not available at the time of printing, the estimated percentage is based on the following: Gap for 1988 of 26.28 percent minus the January 1989 increase of 4.1 percent plus the changes in the White Collar Less Sales ECI from March 1988 to March of 1989 of 4.8 percent, rounded.

OPM database, this database is currently the most complete data available for estimating pay differentials for many locations. Future surveys will enable more precise measures of cost.) The Wyatt cost figure includes cost estimates for a nationwide administrative and professional salary schedule, locality schedules for clerical and technical employees and an additional pay differential above the nationwide schedule for professional and administrative employees in Los Angeles, San Francisco and New York.

Exhibit I

SUMMARY OF COST ESTIMATES

Estimates as of March 31, 1988

Metropolitan Statistical Area	Clerical/ Technical/ Other	Professional/ Administrative
Albuquerque	$ 1,644,216	$ 14,263,068
Atlanta	36,207,826	52,875,845
Austin	14,622,121	6,799,385
Baltimore	26,601,788	83,116,278
Boston	8,242,931	42,083,923
Bremerton	11,190,185	12,523,798
Charleston	617,342	10,100,219
Chicago	23,488,389	57,309,295
Cincinnati	4,197,269	8,551,598
Cleveland	3,682,198	17,343,964
Columbus	4,219,811	19,536,836
Davenport-Moline	11,186,056	20,685,174
Dayton-Springfield	10,909,575	58,587,122
Denver-Boulder	35,507,020	54,072,536
Detroit	27,036,219	41,751,857
Dallas-Fort Worth	19,172,803	47,059,067
Harrisburg-Lebanon	11,528,465	25,024,703
Houston	19,034,223	25,499,678
Huntsville	2,613,978	45,880,002
Indianapolis	7,413,224	22,033,723
Jacksonville	3,929,723	11,459,496
Kansas City	18,775,638	35,662,748
Los Angeles	54,801,693	71,270,887
Macon-Warner Robins	2,737,082	25,048,761

Memphis	7,313,054	8,684,907
Miami	1,755,880	17,245,941
Minneapolis-St. Paul	6,109,940	13,929,234
Monmouth-Ocean County	11,571,932	34,308,420
Nassau-Suffolk	13,011,269	13,715,655
New Orleans	3,231,915	15,539,197
New York	24,912,030	65,802,338
Norfolk-Virginia Beach	2,571,567	65,958,541
Oklahoma City	16,547,987	39,213,263
Oxnard Ventura	10,166,764	17,313,745
Philadelphia	39,308,384	92,752,687
Phoenix	5,551,737	10,930,777
Pittsburgh	8,629,373	8,420,683
Portland, Oregon	9,688,092	13,375,494
Richmond-Petersburg	334,336	19,474,338
Riverside-San Bernardino	11,672,844	13,207,394
Sacramento	27,972,315	32,819,374
St. Louis	21,318,373	66,388,521
Salt Lake City-Ogden	17,760,300	32,683,548
San Antonio	9,284,004	55,626,771
San Diego	30,081,359	36,009,660
San Francisco-Oakland	50,786,321	67,177,439
Seattle	13,251,968	23,772,944
Washington, D.C.	319,995,932	727,231,867
	$1,022,187,451	$2,300,122,701

THE PAY POLICY OR ALTERNATIVE COST ALIGNMENT ISSUE

It is common practice in designing a compensation program to define specifically the level of pay to be maintained over time relative to prevailing market levels. This basic decision is often referred to as an employer's compensation strategy or its pay policy. The government's stated policy has been to maintain comparability with private sector pay levels.

There appears to be a consensus that the definition of the relevant labor market should be broadened to include state and local government employers. The effect of this change, however, is unknown at this time.

In addition, the government might want to consider paying more or less than the market average. For example, an employer may adopt a policy to pay salaries which are at the 75th percentile of the market, which would mean, in concept, that the organization's salary program is designed to pay salaries that are higher than three out of four employers in the labor market. Similarly, a firm that is dependent on scientific expertise may decide to pay incumbents in these positions at the 90th percentile to attract the best specialists in the country.

While some employers, by policy, maintain salaries at or above the market average with the expectation that this will allow them to attract and retain higher calibre employees, there are a number of factors which influence this policy decision. In addition to the ability to pay, an employer deciding where to set the salary policy line will consider the relative cost of the benefits package offered, and the attractiveness of internal policies such as rate of promotion, speed of in-range progression, career opportunities, intrinsic attractiveness of the work to be done, and job security. Other factors which can also affect the decision may include quality of facilities, desirability of location, and other progressive personnel policies which make the organization desirable to job applicants, e.g., flexible work hours, dependent care facilities, etc. Some of these factors have a cost attached, while

others do not. However, each of them, to a greater or lesser degree, can be factors in determining the necessary and appropriate level of direct pay.

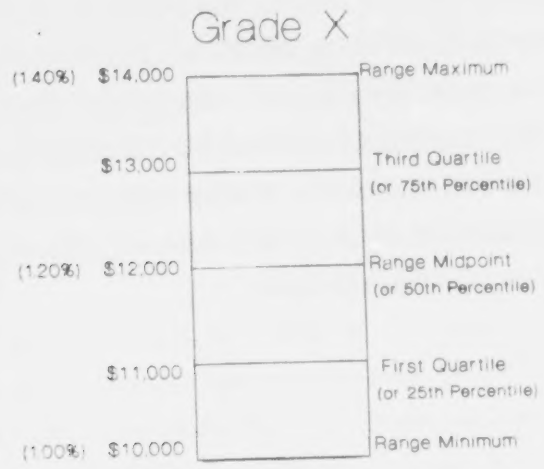
Payroll costs are obviously important to all employers. The quality and productivity of employees has to be balanced against the cost. Employers that design their salary program to pay market salaries have to believe that the increase in costs will be offset by productivity gains. In the same way, employers that pay below market salaries to hold down payroll costs have concluded that they will still be able to recruit enough adequately qualified employees.

Most employers elect to implement this policy decision by establishing a "policy line" around the appropriate market data. If the decision is to maintain salaries at the 75th percentile, these values are extracted from survey data, and used in the regression analysis that generates the line. The salary structure and ranges then are established so that the range midpoints are based on the policy line. This, of course, also establishes the range minimums, and therefore starting salaries.

Unfortunately, the OPM database includes only means and medians, which makes it impossible to calculate estimates based on percentile values (as illustrated in the graph on page 4).

As an alternative (or in combination), it is possible to move the salary ranges up or down relative to the policy line. If linking the midpoints to the line is consistent with a policy to pay average salaries, then a policy line above the midpoint effectively lowers overall salaries, since more employees will be paid below the market averages. Conversely, a policy line below the midpoints effectively increases overall salaries. The federal government will have to make a policy decision as to where in its salary structure it will approach average competitive market rates.

Based on our recommendation to adopt 40 percent salary ranges, the salary ranges will be consistent with the following mathematical relationships:



Following this logic, if the policy line were fixed at the 75th percentile of the ranges, the midpoint of the hypothetical range would be $11,077. To determine this value, we assumed that the 75th percentile of the range was set at the market rate, $12,000. Based on this, the minimum of the salary range has to be $9,231 ($12,000 / 1.30), making the midpoint $11,077 ($9,231 x 1.20). The norm in the private sector in positioning the line is to use the midpoint or 50th percentile of the rate range.

Similarly, if the policy line were fixed at the 70th, 50th, or 40th percentile of each grade range, the midpoints would be $11,250, $12,000, and $12,414 respectively. This logic makes it possible to determine the cost implications of moving the salary structure so that it is aligned with the policy line at any point in the grade range.

For example, setting the policy line at the 70th percentile would reduce our aggregate cost estimate by 6.25 percent (11,250 / $12,000, or 93.75%). This would be a savings of $224M (.0625 x $3.576B). Similarly, setting the policy line at the 40th percentile would increase the cost by 3.45 percent ($12,414 / $12,000 or

1.0345). This translates into an increase of $123M. These estimates pertain only to the 48 MSA's

We are aware that the government has addressed this policy issue in the past and, at each point, continued to support the need to compare average actual federal salaries paid to average salaries in the private sector. However, this issue and the methodology used to implement this policy are important cost determinants. We recommend that the cost implications of alternative policies be considered in-depth, taking into consideration all of the factors which may affect the government's ability to attract and retain qualified employees.

CLOSING THE GAP: THE CASH FLOW IMPLICATIONS

It has taken a decade to create the gap, and it is anticipated that the Congress will decide to phase-in the funds needed to close the gap over several years. Since salaries are normally adjusted annually, with the adjustment paid out incrementally in paychecks, the cash flow can be readily projected. This type of an analysis is complicated by the fact that the gap is a moving target; employers across the U.S. economy also adjust salaries each year. This makes it important to measure the gap each year, and to adjust funding plans to keep pace with salary increase trends.

This analysis emphasizes the need to anticipate labor market trends and "competitive" salary increases. Labor markets are dynamic; salary levels are affected by adjustments spread throughout the year. Most employers use two types of survey information to plan their salary programs: pay rates for individual benchmark jobs and plans for salary adjustments for the next fiscal year. It is important to understand that salary survey data are effective as of a point in time, and that by the time the data are used, the salary levels would have already moved. In using the annual PATC data, the government has ignored this reality.

It is common to make assumptions about salary increase trends in the labor market, and to use the assumptions in analyzing survey data. Our 5 percent increase assumption is consistent with this practice. These assumptions are essential to projections into the future.

Annual surveys of salary increase budgets over the past several years have consistently shown that employers have planned on increases in the 5.0 to 5.5 percent range for white-collar workers. This has been generally true across the

country. (The increases for blue-collar workers have been somewhat less.) There is no reason to anticipate that this trend will change so long as the economy is stable.[4]

For the purpose of this analysis, we have assumed that private sector salaries will continue to increase at 5.0 percent per year.[5] If both the government and the private sector increase salaries at this rate, however, the dollar gap will grow by the percentage increase.

This is illustrated by the following simple comparison:

	Present	Future	Increase
Private Sector Salary	$11,500	$12,075	5%
Federal Salary	10,000	10,500	5%
Difference	$ 1,500	$ 1,575	5%
Increase in Gap		+$75	

The illustration is based on a 15 percent gap, which is approximately equal to our estimated gap for the 48 MSA's. As the calculations show, if the private sector increases salaries 5 percent each year, the government will have to increase salaries by 5.75 percent ($575 / $10,000), or the amount of the gap will continue to grow

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[4]Realistic salary planning also takes into account the effect of turnover on salary levels. When employees terminate or are promoted, the salaries paid to their replacements are normally somewhat lower, reflecting the lower position in the salary range of the new employees. The new employees, of course, may not be eligible for a salary increase for a year. This serves to bring down the average salary levels in surveys.

[5]Salary increase budgets reflect the money set aside for employees who are eligible for increases. If planned budgets call for 5.0 percent increases, surveys will normally show that average salaries increased at a slightly lower rate, depending on the level of turnover or staff expansion. Normally, this rate of increase is used to adjust salary structures. To take this into account in our projections, we would need comparable data for both the survey organizations and the federal government. These data are not readily available, therefore, our projections do not include these adjustments. The net difference would be less than 0.5 percent. Our 5.0 percent assumption is conservative, and arguably reflects a turnover adjustment.

because the federal salaries start from a lower dollar base. As a result, when the same percentage is applied to both sectors, the dollar gap continues to grow.

Our projections are based on the assumptions that, overall, salaries for the current white-collar work force will have to increase at approximately 6 percent per year to hold the gap constant. Closing the gap will require increases in excess of this rate.

For budgeting purposes, salary increases are paid out throughout the year. For example, a $1,000 increase in an annual salary is paid out at a rate of $83.33 per month. Therefore, payments started at the beginning of a fiscal year will require the full $1,000 in the budget, while payments started at mid-year will require only $500 in the budget. This is a cash flow issue. While we are aware that the government has deferred increases in the past to hold down the budgeted cost, we do not believe that increases should be delayed because of this.

On this basis, we project that the 6 percent salary increase for the payroll in the 48 MSA's (to hold the gap constant) will cost:

	Payroll	Salary Increases
October 1, 1989	$23.852B	$1.431B
October 1, 1990	25.283B	1.517B
October 1, 1991	26.800B	1.608B
October 1, 1992	28.408B	1.704B
October 1, 1993	30.113B	

To reiterate, the payroll shown covers 55 percent of the white-collar work force.

Closing the gap will require funding in addition to these amounts. The following amounts represent the cost to close the gap over three, four, and five-year periods.

The calculations are based on an initial gap of $3.576B.

Date of Adjustment	3-Year[6] Period	4-Year[6] Period	5-Year[6] Period
October 1, 1989	$1.192B	$894M	$715M
October 1, 1990	$1.192B	$894M	$715M
October 1, 1981	$1.192B	$894M	$715M
October 1, 1992	----	$894M	$715M
October 1, 1993	____	____	$715M

Based on these calculations, the combined salary increase needed as of October 1, 1989, if, for example, the plan is to close the gap in four years, will have to be $2.325B, which represents a 9.7 percent increase. (This figure relates to the employees in the OPM database.) This percentage will go down slightly each year since we are closing the gap with a fixed dollar amount each year, while salaries are increasing.

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[6]These numbers may be overstated because they do not take into account the recommended policy change which would shift salary increases above market rates from the virtually automatic step increases to merit pay.

Closing the pay gap, of course, does not need to be funded on this basis. If the basic salary increase is 6.0 percent per year, it would be possible to close the gap with an amount that represents a constant percentage of the aggregate salaries. This would make the initial payouts smaller in absolute dollars. We anticipate that the budget deficit will dictate the basis for closing the gap.

COMMENTS ON A PHASE-IN STRATEGY

It is not our role to decide how much the government can afford to spend. While we believe our aggregate cost estimates are reasonable in light of the database limitations, we are very much aware of the need to refine the cost estimates with new survey data, and also of the need to "clean up" the classification and grading problems. However, this additional work will take two or more years, and we believe the government cannot afford any further delay, especially in some locations and for some occupations.

Accordingly, we strongly recommend that the Congress and the Administration rely on our data analysis to confirm the magnitude of the problem. In our opinion, the database is fully adequate to make the basic "business decisions" needed to establish a framework for a new salary program. Assuming that the cost will necessitate a multi-year phase-in for the new program, it would be practical to complete the supplemental surveys and analysis early in the phase-in period. With appropriate scheduling and planning, the studies could be complete well in advance of the final catch-up adjustments.

To emphasize this point, there is a definite sense of crisis that is shared by key individuals across government. Delaying the needed changes will definitely exacerbate the problems. Under the best of conditions, salary programs are based on imperfect information. The conceptual framework for a new program is important, and needs to be carefully considered, but additional survey data will not change the basic conclusions. We recommend that government act on our recommendations as quickly as possible.

While the precedents and thoroughly tested concepts relevant to the design and administration of salary programs exist, there is no information that could be similarly useful in planning the phase-in strategy. The transition from the current program to a new one will presumably require an increase in funding so the phase-

in strategy will specify how the "new" money is to be allocated. These decisions will be discretionary but from our perspective should reflect the government's priorities and perceived importance of problem areas and/or occupational groups.

A basic consideration is the allocation of the new money between the local Clerical/Technical salary programs and the national Administrative/Professional program. Of the two, our discussions suggest that the Clerical/Technical programs should be the first priority. The Clerical, Technical, and Other series job openings, are often difficult to fill in some cities. The government cannot rely on the attraction to public service; the jobs have to be filled and the work needs to be performed. Higher salaries in some locations should immediately enhance the qualifications of job applicants. Equally important and requiring priority attention are the pay levels for Professional/Administrative positions in the very high labor cost MSA's and the entry level salaries overall. As we note in the Task 3 Report, the government entry level salaries for college graduates are significantly below the national average.

On a related issue, in some areas, the salaries currently paid to the Clerical, Technical and Other series employees are still competitive with, if not above, the market. While we have recommended that these salaries should not be cut, it will be important to adopt a strategy to bring the pay levels in these areas back in line with the local market. We recommend that the employees be granted annual increases equal to one-half of the local budgeted increases planned by other employers in the local area. For example, current salary increase budgets are in the 5.0 to 5.5 percent range. Our recommendation would mean that employees in areas where the federal policy line is above the comparative local pattern would be eligible for 2.5 to 2.75 percent. (Under our recommendations, employees currently at step 7 or above would be eligible for merit increases that should also be reduced by 50 percent.) This policy would be continued until surveys show that federal salaries are in line with the local market.

There is, of course, no economic reason, where federal salaries are above the local market, for granting anything more than the normal step increase. Alternatively, salaries could be frozen until local salaries are increased to federal levels. However, this policy would adversely affect employee relations and union support for the proposed program which is the reason for the recommendation to continue modest salary increases.

Another phase-in strategy would be to allocate any "new" money to the MSA's where the pay gap is the largest. Having met with the Federal Executive Board in New York, we are aware that any delay in salary increases for this area will aggravate an already critical situation. We can only presume that the recruiting and retention problems in the other high pay areas are equally serious. The OPM database is sufficiently valid to justify immediate action in these areas.

Similarly, for essential occupations where the supply of appropriately qualified applicants is inadequate, special increases could be authorized. The database provides a basis for estimating market levels, and since this is a moving target, the initial catch-up adjustments do not require precise market data.

To reiterate, the government has considerable discretion in planning and implementing the phase-in strategy. It will be important to confirm our conclusions with statistically valid survey data, but the absence of better data does not have to, and should not, delay approval of the recommended program changes. The increased funding to close the gap can be spread over as many years as necessary, but the faster the gap is closed, the sooner the negative image of federal careers can be reversed. The government will have to establish priorities, and it may prove to be difficult to develop a consensus on this issue. There are no relevant precedents.

RESPONSES TO SUPPLEMENTAL OPM QUESTIONS

The contractor should define:

- each geographic area, and criteria for determining geographic boundaries, as well as ways of redefining such areas to maintain the system;

It is impossible to define the areas precisely at this time since survey data are available only for MSA's. We are essentially recommending the FWS "area of application" concept be used as a model. However, we are convinced that the new program will not require 135 separate areas. In practical terms the program should be based on geographic areas where the "local labor market" dictates generally consistent salary levels for similar jobs. Separate areas will need to be established for a number of urban areas, but broad rural areas, particularly in the midwest, can probably be covered under the same salary schedule.

There are no universally applicable criteria for defining labor markets. Counties, however, have proven to be acceptable for the FWS program. We recommend that the new program follow this practice. Using the existing AWS geographic areas as a starting point, it should be possible to expand selected areas to include additional counties.

If the areas are as broad as we anticipate, with an initial focus on urban areas and the AWS boundaries, there should be little reason to redefine them. Labor markets do change over extended periods as the population increases; however, this is a gradual evolution that takes years before it would justify a redefinition of the survey areas.

The commonwealths and territories mentioned--Puerto Rico, Guam, the Virgin Islands, Samoa, and the Northern Marianas--should have separate local salary programs for Clerical and Technical employees, based on local surveys. These

workers are normally local residents, and the government needs to be competitive with other local employers.

Conceptually, the Professional and Administrative employees in these territories should be paid under the national schedule, with geographic differentials if warranted by local prevailing pay levels. However, we recommend that surveys be conducted in each territory to compare local salary levels with the levels dictated by the revised national schedule. Corporations with operations in those areas would commonly provide allowances for cost-of-living, education, etc. to expatriates; therefore, the government's survey will need to confirm how the major employers compensate their professional and administrative employees.

- Occupations and grade levels to be included/excluded from each area;

Our recommendation is to administer the salaries for Clerical, Technical and Other series under local salary programs. The relevant grade levels are those applicable to these services; the grades that would be excluded are those in each area that do not have incumbents in these series.

We have recommended that the health care specialists and law enforcement series be pulled out of the GS program, and separate occupationally-specific pay programs be established. We also have recommended that the salaries for research positions be administered under a broad band concept so they would no longer be covered by the current grade structure.

- Standard Industrial Classification (SIC) codes or industrial scope of each survey, including size of establishments;

There are differences in the industrial scope of the PATC and AWS surveys. At this juncture there are very few industries which are not included in the population from which the PATC sample employers are selected. The only major

industries excluded from the PATC definition are: (1) agriculture, (2) U.S. Postal Service, (3) private households, and (4) public administration (Division J). While private health service and educational service employers are included, public employers in these categories are not.

We are recommending that the survey population be broadened to include public administration employers. However, even with this change, it will be important to sample from a fixed set of industries for all areas.

The size issue is less straightforward. While we see no reason, in general, for the government to include small employers in the surveys, there are areas where small employers cannot be ignored in the labor market. BLS has informed us that adding employers with as few as 50 employees, at least in the urban areas, has a negligible impact on results. We believe that the 200 or more employee criterion should be satisfactory, but this is an issue that the BLS should address in planning the surveys.

- Construction of the pay schedule(s), and/or differentials; number of grades, sizes of each, and overlap of ranges; role of differentials;

At this time we are recommending no changes in the construction of the schedules, except for the increase in the range from 30% to 40%. Our recommendation is to adopt this increase in the range "spread," to treat step 7 as a "midpoint," and to rely on merit pay above this.

It would be useful to consider other changes but this would be analogous to opening the proverbial Pandora's box. If, for example, the number of grades were changed, every position would have to be assigned to a new grade. The locality pay program should be implemented first.

At some later date we recommend a review of the percentage differentials between salary ranges. There is no right answer but the practice in industry is to rely on differentials in the 8 to 12 percent range, which is significantly less than the differentials reflected in the General Schedule. This change would increase the number of grades, and we believe this would be advantageous to the government.

We have recommended geographic differentials for the Professional and Administrative series where prevailing pay levels are significantly above the national "norm." It would definitely be more advantageous to pay special "add-on" differentials in a small number of locations than it would be to increase salaries across the country to match salaries in the high pay areas.

Each local salary program for Clerical and Technical workers would be free to "float" with the local market. There would, therefore, be no need for differentials.

- The relationship of possible bonuses, e.g., retention, recruitment, or other bonuses, the local pay schedules;

While corporations often use recruiting and retention bonuses (with the latter treated as year-end performance bonuses), this practice is generally limited to executive and managerial positions. It will be advantageous to authorize limited use of recruitment and retention bonuses until the salary schedules are fully competitive. However, the concept should be used selectively as it has potential for abuse.

- The relationship of turnover and vacancy data to the need for changes to the schedule(s).

In our opinion, there has been far too much emphasis on turnover and vacancy data, and too little on the quality of job applicants. In a number of our meetings individuals commented on the declining qualifications and apparent abilities of

federal applicants. Unfortunately, there has been little evidence compiled to confirm this problem.

There is a widely-held belief in the private sector that comparatively high salaries make it possible to attract better workers. In this context, the comparative value of the total compensation package is believed to be important in recruitment. Many employers reflect this belief in the design of their compensation and benefits programs.

If higher salaries enhance a firm's ability to recruit well-qualified employees, it is reasonable to assume that the converse is also true. Our experience leads us to believe that the quality of the government's work force has to have been adversely affected over the past decade.

We are not aware of any private sector employers that explicitly consider either turnover or vacancy data as criteria for adjusting their salary programs. If employers begin to experience either problem, they might initiate the study needed to determine whether salary levels are responsible, but this would only be in reaction to a perceived problem.

Private sector employers commonly adjust their salary programs annually. The 1989 Survey of Locality Pay Practices in Large U.S. Corporations, contained in Task 2, reports that 80 percent of the respondents follow this policy.

We appreciate that the government's size makes it easier to collect and thus emphasize quantitive work force data but data on the quality of the work force is much more meaningful.

- An assessment of how the system could be administered and the various ways that necessary decisions can be made to ensure smooth operation of the new system.

Our recommendations represent, in our opinion, a conceptually simple program that should be relatively easy to administer. It will be necessary initially to define the local areas and conduct the necessary surveys. This should be the responsibility, jointly, of OPM and BLS.

We anticipate that there will be an ongoing need to discuss national procedural issues, to periodically review the geographic definition of the local areas, and to monitor local salary program adjustments. This may necessitate the creation of a committee or group similar to the Prevailing Rate Advisory Committee.

We do not believe it will be necessary to conduct surveys annually. Our recommendation is to conduct the local surveys every three years, with interim adjustments based on ECI data. The three-year cycle should enable BLS to balance its work load by allowing it to schedule the surveys for one-third of the areas per year.

However, it should be feasible to have BLS design and monitor the surveys, with actual data collection being done by local agency personnel specialists. This approach represents a compromise between the centralized approach used with the Area Wage Surveys, and the decentralized Federal Wage System approach. To reiterate from our Task 4 recommendations, we do not believe the private sector will cooperate with the government in the new surveys, if union representatives accompany the data collectors. Moreover, the geographic areas will differ from the FWS areas so the survey effort will have to be independent. It would, however, make sense to have locally - controlled data collection so long as it is carried out within BLS-dictated procedures.

The OPM staff, in turn, will have to decide if it wants to delegate responsibility for analyzing and interpreting the survey results, and for completing the calculations needed to adjust the local salary schedules. This must be done consistently across the country, but could be delegated with adequate policy and procedure controls.

Once the structures are created, and the adjustment methodology established, there are only two types of administrative issues: position classification and, if approved, merit pay actions above Step 7. Although there will be a need for inter-agency monitoring of these actions, we see no reason to create new administrative units at the local level. (A broadened merit pay program will need an appropriate administrative structure.) However, we anticipate that the regional OPM offices will have reasons to coordinate and monitor the local programs. In some respects, this role is analogous to the position of local compensation manager, found in most multi-location corporations.

Corporations frequently delegate responsibility for data collection and analysis, and permit local managers to formulate recommendations related to program administration. The parent company staff, however, often retains the final approval authority. We recommend that OPM consider this approach to program management.

APPENDIX

DESCRIPTION OF STATISTICAL METHODOLOGY

The policy line regressions for the 48 MSA's were computed using the statistical program SAS, running on an IBM style mainframe. The data was provided by OPM, and the variables used are as follows:

- locavg — Private sector local average salary, reported by job and grade level.
- locees — Private sector employment levels, reported by job and grade level
- fedavg — Federal government average salary, reported by job and grade level.
- fedees — Federal government employment levels, reported by job and grade level.
- patco — Dummy variable equal to "CT" for clerical and technical jobs, and "AP" for administrative and professional jobs.
- msa — Variable designating MSA.
- festot — Total FES points for each job and grade level.

In discussion with OPM, it was decided to eliminate all observations for which the reported local mean salary was less than $7,000 a year, since this would have implied that the hourly wage was less than the minimum wage. Further, for jobs for which an FES total was not available, a first order correction would be used. That is, the average FES total by grade level and patco category would be used.

With these corrections made to the data, the following model was estimated:

$$\text{locavg} = B_0 + B_1 \text{ festot}$$

by patco, msa
weight locees

Where the Beta's (B) are the parameters being estimated.

Separate regressions were run for the two patco categories, by MSA. An important consideration was the use of the variable locees as a weighting factor. Basically, the concept is that the higher the employment level of a job (by grade), the more important it would be in determining the policy line. A brief description follows. For a complete explanation of weighted regression analysis, refer to the SAS User's Guide: Statistics, or to Judge, et al, The Theory and Practice of Econometrics.

The federal line was estimated, not taking into account patco or msa, using federal employment levels as the weight:

$$\text{fedavg} = B_0 + B_1 \text{ festot}$$
$$\text{weight fedees}$$

Finally, the proposed national line used for the costing analysis was estimated for the professional and administrative jobs (patco = 'AP'). Excluded from the data were the cities of New York, Los Angeles, and San Francisco. The model estimated was:

$$\text{locavg} = B_0 + B_1 \text{ festot}$$
$$\text{weight locees}$$

WEIGHTED LEAST SQUARES REGRESSION

Let n be the number of observations, and k be the number of independent variables. Then, let the following symbols denote

Y A n x 1 matrix consisting of the values of the dependent variable (in this case either locavg or fedavg).

X A n x k matrix consisting of the values of the independent variable (in this case festot).

W A n x n diagonal matrix consisting of the values of the weights (in this case either locees or fedees).

In ordinary least squares regression, the parameters to be estimated are the solutions to the following matrix equation:

$$B = (X'X)^{-1} X'X$$

In weighted least squares regression, the parameters to be estimated are the solutions to the following matrix equation:

$$B = (X'W X)^{-1} X'W Y$$

For a complete explanation of weighted least squares regression, see Judge, Griffiths, Hill, Lütkepohl, and Lee, The Theory and Practice of Econometrics. John Wiley and Sons, 1985. For an explanation of how SAS implements weighted least squares regression, see SAS User's Guide: Statistics, SAS Institute, Inc., 1985.